
Hotel Conference Center Feasibility Study

Proposed New Downtown Hotel Conference Center

Flagstaff, Arizona

Prepared by:

HVS Convention, Sports & Entertainment Facilities Consulting
445 West Erie Street, Suite 110
Chicago, Illinois 60610
(312) 587-9900
(312) 587-9808 FAX

Submitted to:

Mr. Chris Anderson
Project Manager
Hines
2375 E. Camelback Road, Suite 790
Phoenix, Arizona 85016
(602) 385-6900

August 4th, 2004

Table of Contents

Section	Title
1	Summary of Salient Conclusions
2	Nature of the Assignment
3	Site & Facility Program Review
4	Market Overview
5	Industry Trends
6	Comparable Facilities
7	Group Event Demand Analysis
8	Hotel Supply & Demand Analysis
9	Projection of Occupancy
10	Average Rate Analysis
11	Financial Operations
12	Assumptions & Limiting Conditions
13	Certification

1. Summary of Salient Data and Conclusions

Site	Property:	Proposed Hotel Conference Center
	Location:	Downtown Flagstaff between Verde Street and Elden Street at the eastern terminus of Aspen Street
	Date of Inspection:	February 12 th , 2004
Project Description	Anticipated Date of Opening:	April 1 st , 2006
	Property Type:	Hotel Conference Center
	Gross Square Feet:	256,000
	Facility Description:	A 250 room full-service hotel conference center with approximately 25,000 net square feet of IACC certified meeting and banquet space. The City of Flagstaff, or its representative authority, would own the hotel conference center and Benchmark Hospitality would operate it.
	Parking:	In conjunction with the hotel conference center development, the City plans to develop structured parking spaces adjacent to the facility. The new structured parking facility would have approximately 400 parking spaces.
Conclusions	The proposed subject property will be extensively marketed as a destination conference center and will rely upon capturing meeting and group demand from corporations and associations based primarily in Central Arizona and Northern Arizona.	

Due to its location along Interstate 40 and proximity to the Grand Canyon, Flagstaff as a destination attracts a majority of leisure transient demand, particularly during the peak summer travel months. Recreational attractions in the area also have the capacity to attract leisure visitors during the winter.

Marketwide hotel occupancy levels rose to a peak of 68.8% in 2003. Average rates have grown slightly over that period from \$91.66 in 2001 to \$95.05 in 2003; resulting in steady RevPAR growth during this period.

Conference activity currently is limited in the Flagstaff market. Based on interviews and surveys, this is largely due to the lack of a suitable facility for upscale meetings, conferences, and conventions. The DuBois Center at Northern Arizona University hosts a small number of educational and research related conferences and meetings each year. Among hotel properties, Little America and Radisson Woodlands Hotel are the market leaders that accommodate the vast majority of meeting and group demand generated within Flagstaff. These hotels compete with hotels in Prescott and Sedona for drive-in business from Phoenix and other areas around the state.

The market for transient commercial and leisure accommodations in Flagstaff is traditionally price-sensitive. Area property managers have indicated that the unwillingness of many guests to pay premium rates for lodging is a major reason why the market lacks high-quality, full-service lodging facilities. Sedona is a higher-rated destination due to the resort nature of the town, and to the views and recreation opportunities afforded by the Red Rocks formations.

The 219-room Hilton Sedona Resort & Spa is the average rate leader in the market, at \$138.00 in 2003, and Little America is the leader in occupancy level, at 73.0% in 2003. The market demand has a leisure orientation with this segment comprising 52% of total lodging demand in 2003.

HVS evaluated the demand potential for the proposed new hotel conference center in downtown Flagstaff. HVS projects annual demand potential for over 1,300 meetings and conferences in a stable operating year. These events are expected to represent total annual attendance of more than 83,000 people in a stable year of operation.

Induced meeting and group demand is forecast to grow from roughly 7,000 room nights in fiscal year 2006/2007 to more than 17,000 room nights in fiscal year 2009/2010, the stabilized year of operation. Most of the induced room night demand will be generated by groups that will use the meeting and conference space proposed for the subject facility. We forecast a minimal additional amount of induced demand in the leisure and commercial segments.

We anticipate that the market will quickly absorb the proposed subject property's rooms and marketwide occupancy is projected to reach the low-70% range within three years of the proposed subject property's opening.

The HVS analysis projects a stabilized occupancy level of 65% in the fourth year of operation for the proposed property. The stabilized average daily rate deflated to current dollars equates to \$146.41. Compared to the subject property's anticipated first-year average daily rate, deflated to current year dollars, of \$133.30, our forecast indicated real rate growth of \$13.11 through the stabilized year.

We estimate that conventional property taxes for the proposed conference center hotel would equal roundly \$523,000 in the first projection year, increasing to roundly \$572,000 in the stabilized year. For the purposes of this analysis we have not included property taxes during the first 8 projection years and included property taxes in the 9th and 10th years, adjusted only for inflation from the stabilized year. We note that this is a preliminary estimate subject to change.

Financial projections for the subject property indicate total revenue is expected to increase from approximately \$11.5 million in the first operating year to nearly \$17.8 million in the first stable year of operations. Net operating income is projected to grow from roughly \$1.5 million in the opening year to approximately \$5.0 million in the first stable operating year.

2. Nature of the Assignment

Subject of the Study	<p>The subject of the study is a proposed new hotel conference center in Flagstaff, Arizona. Hines retained HVS to test the feasibility of the concept and to generate financial operating projections for the subject project. HVS studied the development of a hotel conference center with approximately 250 guestrooms and 25,000 square feet of rentable meeting and banquet space.</p> <p>A 400 stall parking structure is also planned in conjunction with the development of the hotel conference center. HVS conducted a feasibility study for the hotel conference center. The study analyzes Flagstaff's market potential for hotel and event demand. HVS projections indicate potential for events and room night demand. This study also provides financial projections for the subject hotel conference center. The hotel and conference space will be managed by a single operator. HVS provides a single, unified study that analyzes both the hotel and conference center components of the proposed facility.</p>
Objective of the Study	<p>The objective of the study is to identify and evaluate the supply and demand factors affecting the market for meetings, conferences, banquets, conventions, and room nights in the Flagstaff market area. This analysis is intended for the purpose of developing a forecast of event and room night demand and financial operations for the proposed facility.</p>
Use of the Study	<p>This study has been prepared for use by the client for the purpose of developing a hotel conference center in Flagstaff, Arizona. None of the enclosed materials may be reproduced in any form without our permission. If the reader is making a fiduciary or individual investment decision and has any questions concerning the material presented in this report, it is recommended that the reader contact us.</p>
Method of Study	<p>The method of study includes an analysis of key demographic trends and economic data, a review of industry trends, an analysis of comparable facilities, a review of the proposed site and facility program, survey</p>

	<p>research, event demand estimates, an analysis of hotel supply and demand, projections of average rates and occupancy, and financial operating projections for the proposed development.</p>
Ownership and Management	<p>The proposed hotel conference center will be owned by the City of Flagstaff, or an authority representing the City. Benchmark Hospitality will operate the hotel conference center. A qualified management agreement between the owner and the operator will detail management and booking policies. Based on current plans, HVS assumes the hotel conference center will be independent and will not carry a national flag brand name. The project will be branded as the Grand Flagstaff Hotel Conference Center, a Benchmark Hospitality operated facility.</p>
Date of Inspection	<p>The proposed site for development was inspected by Stephen O'Connor, Elaine Sahlins, and Hans Detlefsen on February 12th, 2004.</p>
Assignment Delivery	<p>HVS presents this report as the product of our research and analysis concerning the market and feasibility of the proposed hotel conference center in Flagstaff, Arizona. This report includes financial operating projections based on our analysis of event and room night demand for the subject. After a thorough review by the client, HVS has finalized this report and submitted it as a final document to the client.</p>

3. Site and Facility Program Review

Description of Site

The suitability of the land for the operation of a lodging and conference facility is an important consideration affecting the economic viability of a property and its overall feasibility. Factors such as size, topography, access, visibility, and the availability of utilities have a direct impact on the desirability of a particular site.

The subject site is located within Flagstaff's central business district at the eastern terminus of Aspen Street between Verde Street and Elden Street. Municipal jurisdictions governing the property include the City of Flagstaff, Coconino County, and the State of Arizona.

Picture 3-1 shows views of the subject site from Aspen Street.

Picture 3-1

Views of the Subject Site Facing West



Picture 3-2 shows views of the subject site from Birch Street and Elden Street.

Picture 3-2
Views of the Subject Site Facing Southwest



Picture 3-3 shows views of the subject site from Verde Street.

Picture 3-3
Views of the Subject Site Facing Southeast



The subject site is currently occupied by an automotive dealer. The City has entered into negotiations with the current land owner to discuss the possibility of a land swap. This negotiation process is ongoing. But the City does not anticipate there will be a problem obtaining control of the site.

Facility Program

As with site selection, the selected facility program is also very important. The facility program can dictate the ability of a hotel conference center to serve different types and sizes of events. Facility program elements such as meeting rooms, banquet space, food and beverage services, guestrooms, and pre-function space have a direct impact on the performance of a particular building.

Table 3-1 shows the proposed facility program for the subject hotel conference center.

Table 3-1
Preliminary Facility Program

Area Description	Net Square Feet	Gross Square Feet
Guest Rooms and Corridors	137,190	143,532
Conference Area	37,326	38,274
Conference Services	1,495	1,620
Lobby	4,714	5,559
Front Office	1,454	1,670
Accounting	1,332	1,470
General Office	3,767	4,114
Conference Dining	5,823	6,503
Pub / Bar	3,165	3,290
Kitchen	5,433	5,673
Purchasing and Storage	2,558	2,672
Receiving	1,260	1,440
Employee Facilities	2,104	2,203
Human Resources	422	466
Fitness Center	7,509	8,079
Housekeeping	3,517	3,674
Maintenance	1,046	1,068
Miscellaneous	20,389	24,548
Total Square Feet	240,504	255,855
<i>Source: Hines</i>		

The proposed hotel conference center will include 250 guest rooms and suites. The preliminary facility program also includes a grand ballroom of

approximately 7,800 square feet. This program also includes 14 smaller conference breakout rooms. A large spa and fitness center will include lockers and changing rooms and will be open to resident members. The full-service property will also include a conference dining area and a separate bar / restaurant on the main level. A full-service catering kitchen will serve both the hotel and conference areas. The proposed facility includes approximately 256,000 gross square feet of hotel and conference space.

4. Market Overview

The purpose of this section is to review key demographic and economic trends that have implications for event demand in Flagstaff. This market data will provide insights about the potential to generate demand for the subject hotel conference center. Economic and demographic trends in Coconino County will influence future demand for meetings, conventions, conferences, and other group business in the Flagstaff market area. This section of the report analyzes economic data concerning Flagstaff and the surrounding area.

Market Areas

The City of Flagstaff is located in northern Arizona in Coconino County. It lies approximately 140 miles north of Phoenix at the convergence of Interstate 17 and Route 66. Flagstaff is considered a gateway to the Grand Canyon, which is located approximately 75 miles north of Flagstaff. With a population of approximately 60,000 people, Flagstaff is the largest City in the northern third of Arizona and the only metropolitan area in the state north of Phoenix. Several smaller destinations between Phoenix and Flagstaff include Prescott, Camp Verde, Cottonwood, and Sedona.

Flagstaff serves as a commercial hub for several surrounding towns in Coconino County such as Pine Springs, Williams, Bellemont, and Winona. It is also a regional hub for government offices such as the National Forest Service. Moreover, Flagstaff serves as a seasonal destination for residents in the southern portions of the state who seek a respite from hot temperatures in the valley during the summer. With an elevation of approximately 7,000 feet, Flagstaff has a considerably cooler climate than Phoenix and other areas in the southern part of Arizona. Cool summer temperatures and snow in the winter has made Flagstaff a regional destination for skiers and outdoor enthusiasts. Its location along the historic Route 66 and its proximity to the Grand Canyon also make Flagstaff a national pass through destination for tourists. The climate, historical significance, and recreational opportunities in and around Flagstaff represent a potential advantage for attracting group events from around the Arizona and neighboring states. Northern Arizona University is also a major

element of the Flagstaff population and economic base. As a college town, Flagstaff has a relatively young average age and a distinct creative influence that is reflected in the mix of amenities, entertainment options, and nightlife available in town.

The market areas for most hotel conference centers include two components:

- The local district—the neighborhood immediately surrounding the facility plays an important role in determining the quality of the experience of event planners and attendees. A downtown district or neighborhood that is attractive, well maintained, convenient, and otherwise welcoming to visitors is important for the success of hotel conference facilities.
- The market area—this larger area, usually the surrounding county or counties, provides the base of demand for local events such as banquets and private parties. It supports the downtown core or neighborhood surrounding the facility by adding to the resources available to provide and maintain a community’s visitor infrastructure and attractions in the region.

This study analyzes both components of the market area for the proposed Flagstaff hotel conference center. The analysis will provide the foundation for assessing demand potential for certain types of group events as well as transient hotel demand.

Local District Description

The conditions of the neighborhood directly surrounding upscale conference centers play a large role in shaping visitors’ perceptions of the facility and the community. Hotel conference centers typically serve group business as well as upscale transient demand. An adequate mix of banquet and meeting space allows such facilities to serve out-of-town groups as well as local users and guests from neighboring communities seeking meeting space. The ability of downtown Flagstaff to afford local users and visitors with a comfortable, yet unique, experience is important to the attractiveness and long-term success of the proposed facility.

The selected site for the subject center is located at the east end of the historic downtown area. The site is bound by Verde Street on the west and Elden Street on the east. The proposed facility will be located south of Birch

Street and north of Route 66. The City of Flagstaff has negotiated an option to own the site as the result of a land swap with the current owner. A parking structure with office space is also planned across the street from the hotel conference center. This adjacent development would occur on the southwest corner of Aspen Street and Verde Street, just west of the proposed hotel and conference facility.

Downtown Flagstaff is a Main Street community. Ongoing capital investments and an active small business community make this an attractive area of town, offering a broad mix of shopping, entertainment, dining, and professional and government services. Approximately 10 public agencies and 170 commercial businesses are located in the dense 36-block area defined as the historic downtown district.

A recent streetscape renovation has been completed on the north side of the downtown area. Improvements include street banners and public benches. The Flagstaff Visitors' Center is also located downtown in the recently renovated Flagstaff Railroad Depot along Route 66. Additional downtown development plans include the construction of a new federal building to house nearly 200 government workers and a \$100 million mixed use development that will include office space, retail, government, and commercial space. Bank One and a federal court will be anchor tenants for this 100,000 square foot downtown development. The proposed hotel conference center is planned as a critical component of continued success in the redevelopment of downtown Flagstaff. It would offer the largest and highest end supply of guestrooms in the community and would provide a high-end conference space for statewide conventions, local corporate and government meetings, local and regional banquets, and other group events.

Local Business Climate

The density and character of local businesses largely determines the level of demand for local corporate events such as training seminars, corporate meetings, sales meetings, awards banquets, and other similar events. Upscale conference centers near major urban markets such as Atlanta and Chicago have specifically targeted this segment for a substantial portion of their group business. Flagstaff has a limited supply of major corporations. But some demand may derive from the greater Phoenix metropolitan area. While this demand will be limited due to Flagstaff's distance from Phoenix,

the subject center could still attract multi-day corporate meetings and events.

Table 4-1 shows the largest employers in Flagstaff, as reported by the Flagstaff Chamber of Commerce. These employers have at least 100 full-time equivalent workers.

Table 4-1

Largest Employers in Flagstaff

<u>100 - 249 Employees</u>		<u>250 - 499 Employees</u>	
Employer	Sector	Employer	Sector
Albertson's	Retail	Coconino Community College	Education
Arizona Daily Sun	News	Grand Canyon Railway	Tourism
Dillard's	Retail	Little America	Hospitality
Flagstaff Athletic Club	Leisure	N.A.C.O.G.	Government
Fry's Food & Drug Center	Retail	SWCA, Inc.	Manufacturing
Guidance Center	Healthcare	National Forest Preserve	Government
HomeCo ACE Home Center	Retail	Walgreens	Distribution
Home Depot	Retail	Walmart	Retail
New England Business Service	Telemarketing	<u>500 - 999 Employees</u>	
Nestle Purina	Manufacturing	Employer	Sector
The Peaks	Healthcare	City of Flagstaff	Government
Penney, J.C.	Retail	Coconino County	Government
Nackard Bottling Co.	Distribution	<u>1,000+ Employees</u>	
Radisson Woodlands	Hospitality	Employer	Sector
Safeway	Retail	Flagstaff Medical Center	Medical
Sears Roebuck & Co.	Retail	Flagstaff United School District	Education
Sturner & Klein	Telemarketing	Northern Arizona University	Education
U.S. Geological Survey	Government	W.L. Gore & Associates	Manufacturing

Source: Flagstaff Chamber of Commerce

Employment in Flagstaff is heavily dependent on government and education as well as the service sector. Some major manufacturing firms and distribution centers provide a modest number of industrial jobs in the area. Hospitality and tourism also employ a substantial number of full and part-time workers. But many of these businesses employ fewer than 100 people.

Northern Arizona University is Flagstaff's largest employer, with approximately 2,600 full-time employees. W.L. Gore & Associates is the largest private sector employer in Flagstaff with a current employment base of approximately 1,000 people. Although the largest employers are in the education and manufacturing sector, one area of strength for the Flagstaff economy is its broad base of small businesses in the tourism and hospitality

sector. Numerous hotels, motels, leisure, and tour companies continue to thrive as visitors arrive for skiing and recreation. The climate, Route 66, and the destination appeal of the Grand Canyon have a particularly large influence on the success of this economic sector. The addition of more group event business and out-of-town conferences would complement and augment this sector of the Flagstaff economy.

Hotel Supply

The supply of guestrooms in a community can provide general insights about the health and stability of a local economy. It can also help us understand the existing makeup of the local visitor market. The total supply of guestrooms in Flagstaff is relatively large for a community of its size. A substantial number of independent motels are located along the Route 66 corridor and focus on summer leisure demand.

The quality of hotel properties in the Flagstaff market currently ranges from independent rooms-only motels to full-service properties such as the Radisson and Embassy Suites. Room counts range from eight rooms at the downtown Weatherford Hotel to 248 rooms at the Little America Hotel located on the outskirts of town. The addition of the subject hotel conference center would be the largest and most upscale hotel property in Flagstaff. It would be the only four-star property in the Flagstaff market.

Table 4-2 shows the variety of hotel rooms in Flagstaff and their respective room counts.

Table 4-2
Flagstaff Hotel Room Supply

Property Name	Year Opened	Room Count	Property Name	Year Opened	Room Count
LITTLE AMERICA FLAGSTAFF	1974	246	DAYS INN FLAGSTAFF WEST	1990	57
RADISSON WOODLANDS HOTEL	1990	183	BEST WESTERN KINGS HOUSE MOTEL	1962	57
DAYS INN FLAGSTAFF HWY 66	1964	157	DAYS INN FLAGSTAFF EAST	1991	54
HOLIDAY INN FLAGSTAFF	1987	156	HAMPTON INN FLAGSTAFF	1995	50
MOTEL 6 FLAGSTAFF	1990	150	TRAVELODGE FLAGSTAFF UNIVERSITY	N/A	49
MOTEL 6 FLAGSTAFF	N/A	150	MONTE VISTA HOTEL	1996	48
RED ROOF INN FLAGSTAFF	1987	139	BEST VALUE FLAGSTAFF	N/A	46
FAIRFIELD INN FLAGSTAFF	1990	134	CAROUSEL INN	N/A	44
LA QUINTA INN & SUITES FLAGSTAFF	1996	128	HIGHLAND COUNTRY INN	1983	43
HAMPTON INN SUITES FLAGSTAFF	1998	126	GERONIMO MOTEL	N/A	40
QUALITY FLAGSTAFF	N/A	122	BUDGET INN	1975	38
EMBASSY SUITES FLAGSTAFF	1988	119	ECONOMY INN	N/A	36
AMERISUITES FLAGSTAFF	1993	117	FRONTIER MOTEL	1955	31
INNSUITES HOTELS FLAGSTAFF GRAND CANYON	1980	114	BUDGET HOST INN SAGA MOTEL	1972	30
RAMADA LIMITED FLAGSTAFF EAST	1978	103	RELAX INN MOTEL	N/A	30
MOTEL 6 FLAGSTAFF	1975	103	CHALET LODGE	N/A	30
RESIDENCE INN FLAGSTAFF	1991	102	WESTERN HILLS MOTEL	1960	28
TRAVELODGE FLAGSTAFF	1984	100	TWILITE MOTEL	N/A	28
SUPER 8 FLAGSTAFF SOUTH	N/A	100	SKI LIFT LODGE	1997	26
QUALITY INN FLAGSTAFF	1972	96	ARIZONAN MOTEL	N/A	26
HILTON GARDEN INN FLAGSTAFF	1997	90	WHISPERING WINDS MOTEL	N/A	25
RAMADA LIMITED FLAGSTAFF	1989	89	TOWNHOUSE MOTEL	N/A	25
SUPER 8 FLAGSTAFF	1985	89	WONDERLAND MOTEL	N/A	24
RODEWAY INN FLAGSTAFF	N/A	88	FLAGSTAFF MOTEL	N/A	24
TRAVELODGE FLAGSTAFF	N/A	87	66 MOTEL	N/A	22
COMFORT INN FLAGSTAFF WEST	1990	85	EL PUEBLO MOTEL	N/A	22
BEST WESTERN PONY SOLDIER INN & SUITES	1963	75	CANYON INN	N/A	21
ECONO LODGE FLAGSTAFF	1991	68	FAMILY INNS OF AMERICA	N/A	21
ECONO LODGE FLAGSTAFF	1982	67	AUTOLODGE	N/A	20
SUPER 8 FLAGSTAFF WEST	N/A	66	ARIZONA MOUNTAIN INN	N/A	20
HOWARD JOHNSON EXPRESS INN FLAGSTAFF	N/A	59	THE INN @ NAU	N/A	19
SLEEP INN FLAGSTAFF	1996	58	THE WEATHERFORD	N/A	8

Source: Smith Travel Research, Flagstaff CVB

There are 63 hotel and motel properties with approximately 4,600 guestrooms located in Flagstaff. The community's largest hotel, Little America, is located on Butler Avenue east of downtown. The other full service hotel properties in Flagstaff include Embassy Suites and Radisson. These three convention quality hotels provide 550 guestrooms combined. But they are not centrally located in the downtown area. Multiple limited service hotel properties also offer guestrooms that could serve as overflow supply for some events at the proposed conference center.

The proposed hotel conference center would have an adjoining full service hotel with approximately 250 guestrooms. This would bring the total supply of full-service rooms to 800 in Flagstaff. Moreover, it would bring

the largest and highest quality concentration of full-service guestrooms to the downtown area. The hotel conference center would actively target statewide and regional group events. The property's upscale meeting and ballroom space would also serve local meeting and banquet demand. Benchmark Hospitality is the proposed operator for the hotel conference center. The City of Flagstaff, or an authority representing the City, would likely retain ownership of the facility.

The Flagstaff hotel market experienced a decline in 2001, consistent with national and regional trends in the hospitality industry, primarily attributable to the terrorist attacks and the resultant decreases in leisure travel. The national economic recession in 2001 also led to reduced corporate travel and discretionary spending. Due to the significant drive-in leisure transient component of local lodging demand, occupancy levels did not fall far and have generally returned to stabilized levels ahead of a complete national recovery in the lodging market. However, the higher-rated corporate demand segment has not yet recovered to pre-recession levels.

Local Leisure and Tourism Overview

Flagstaff attracts several million out-of-town visitors annually. The Arizona Office of Tourism commissioned a study in 2001 that indicates annual tourism spending in Flagstaff is approximately \$200 million. The majority of the tourism market in Flagstaff is leisure oriented. Approximately two million people pass through Flagstaff every year on their way to visit the Grand Canyon. This level of visitation and spending is significant compared to the local market population. But it is primarily driven by transient leisure visitors, rather than corporate and group business. Although it is the largest city in northern Arizona, Flagstaff is not currently a statewide or regionally destination for meetings and group events.

Most communities of this size are unable to attract tourism activity on par with major metropolitan areas around the state and country. But Flagstaff has generated a major leisure tourism industry. Shopping, dining, and outdoor recreation are the core of the ongoing success of this industry in Flagstaff. Major leisure attractions, such as the Grand Canyon and the Snow Bowl, will be important assets for Flagstaff in its effort to become a destination for meetings and group business.

Unlike many communities of its size, Flagstaff has been successful at developing its destination appeal for visitors from beyond the local market area. The area's destination appeal, however, is primarily based on its proximity to the Grand Canyon. While this has the potential to be an advantage in recruiting some group business to the proposed hotel conference center, meeting planners currently do not view Flagstaff as a major destination for meetings and conventions. The lack of an adequate conference facility and upscale hotel rooms is a substantial barrier to attracting group business to Flagstaff.

Table 4-3 lists some of the most popular visitor attractions and activities in the Flagstaff area.

Table 4-3

Visitor Attractions & Activities in Flagstaff

Parks & Monuments	Festivals
Arboretum at Flagstaff	First Fridays Art Walk
Coconino National Forest	Holiday Lights Festival
Museum of Northern Arizona	New Year's Eve Pinecone Drop
Riordan Mansion State Historic Park	Flagstaff Winterfest
Sunset Crater Volcano National Monument	Northern Arizona Book Festival
Walnut Canyon National Monument	Grand Canyon Forests Festival
Wupatki National Monument	Flagstaff Summerfest
Heritage Square	Indian Days Celebration
Route 66	Trappings of the American West
Shopping & Entertainment	Wool Festival
The Museum Club ("The Zoo")	Coconino County Fair
Flagstaff Mall	Grand Canyon Music Festival
Historic Railroad Shopping District ("Downtown")	Flagstaff Festival of Science
Sports	Made in the Shade Beer Tasting Festival
Mountain Man Triathlon	Open Studios Festival
Soulstice Mountain Trail Run	Museum & Theater Attractions
Arizona Snow Bowl	Arizona Historical Society Pioneer Museum
Continental Country Club	Flagstaff Symphony Orchestra
Flagstaff Nordic Center	Orpheum Theatre
Pine Country Pro Rodeo	Lowell Observatory

Source: Flagstaff Convention & Visitors' Bureau

Visitor activities in Flagstaff are diverse, including outdoor recreation, shopping and entertainment, festivals, parks, and museums. The most popular area attraction is the Grand Canyon, two hours north of Flagstaff. Historic Route 66 also passes through Flagstaff. Seasonal festivals, the region's only downhill skiing destination (the "Snow Bowl"), and a variety of national forests and parks constitute a significant base of additional

visitor attractions in the area. HVS requested attendance data for these area attractions. However, most destinations did not have estimates or were unwilling to make estimates public.

Based on industry surveys of meeting professionals, HVS has identified several key components that determine the extent and quality of a community’s tourism infrastructure.

Table 4-4 shows several components considered most important. They are not ranked in order of significance.

Table 4-4 Key Elements of Local Tourism Infrastructure	
Destination Characteristics Overall destination appeal History, culture, or unique attributes Number & quality of tourism attractions Natural amenities, geographic resources	Community Image Overall image of community Safety Cleanliness
Visitor Activities Retail attractions Dining / restaurant supply Entertainment options Sports teams, venues, tournaments Recreational opportunities	Visitor Facilities Quality & quantity of hotel supply Quality & quantity of meeting space Transportation access Public Policy Quality & breadth of public services Public commitment to tourism development
Source: HVS International	

Flagstaff’s strongest destination characteristics lie in its natural surroundings, climate, and proximity to the Grand Canyon. Approximately two million tourists visiting the Grand Canyon go through Flagstaff each year. But few major tourism developments in the area attract more than one million visitors on an annual basis. The quantity of hotels is substantial for a market of its size. But the quality of the hotel supply does not include any four-star properties and meeting space is limited. Later in this study HVS discusses how meeting planners view Flagstaff with respect to many of these key tourism characteristics.

Demographic &
Economic Trends

Although there is no direct correlation between population and the demand for conference space, population data can reveal trends in the overall economic climate of an area and its ability to support local meetings and banquets and provide and maintain sufficient visitor-related infrastructure

and attractions. High population or income density and/or growth rates can indicate significant demand potential for local public and private events and a likelihood that the area will add to its existing base of entertainment, retail, and cultural attractions.

Flagstaff is the seat of Coconino County and the largest city in northern Arizona. Although many events held at the proposed center would be statewide or regional in nature, this local market area is the primary source for social, civic, and government events that would generate significant demand for the subject facility.

Table 4-5 shows the population of several communities in Arizona and their distance from, and drive time to, Flagstaff. The table also shows several cities located in neighboring states. Population statistics refer to municipal populations rather than market areas. Market area population statistics appear later in this section.

Table 4-5

Distance and Drive Time to Other Regional and State Destinations

Market	Population (2000)	Drive Time to Flagstaff	Miles to Flagstaff
Statewide Markets			
Flagstaff	52,894	-	-
Grand Canyon	1,460	2:01	77
Phoenix	1,321,045	2:16	145
Prescott	33,938	1:46	95
Sedona	10,192	0:58	29
Tucson	486,699	4:04	260
Yuma	77,515	5:02	322
Regional Markets			
Albuquerque	712,738	4:52	323
Denver	2,581,506	11:34	767
Las Vegas	1,563,282	4:16	252
Los Angeles	16,373,645	6:57	466
Salt Lake City	1,333,914	10:09	519

Sources: U.S. Census Bureau, Mapquest

Flagstaff is roughly two hours north of Phoenix and two hours south of the Grand Canyon. Regional destinations such as Albuquerque, New Mexico and Las Vegas, Nevada are within a five hour drive. Los Angeles, California is within a one-day drive to Flagstaff. An extensive highway

system, including Interstate 17 and Interstate 40, makes this part of Arizona accessible to several major regional markets.

Demographic data such as population, sales, income, and employment statistics provide insight into the general health of the area's economy and its ability to generate locally based event demand. The following tables summarize key economic and demographic data for the Flagstaff market area and Coconino County compared to the State of Arizona and the United States as a whole.

All figures that reflect dollar amounts have been adjusted for inflation by Woods & Poole Economics, Inc. ("Woods & Poole"), a national forecasting service based in Washington, D.C., and thus reflect real changes. The percent changes indicated in the following tables are based on rounded figures and, therefore, may not calculate exactly. The figures presented in the following tables are Woods & Poole estimates and the population figures may vary somewhat from estimates and projections provided by the U.S. Bureau of the Census and local economic development organizations.

Table 4-6 shows historical population growth rates and projections for the Flagstaff metropolitan statistical area ("MSA") which is roughly equivalent to Coconino County. For comparison purposes, HVS shows population trends for the State of Arizona and the United States as well.

Table 4-6
Population Trends Data

Data Type	Period	Data Point	Data Point	Avg. Annual Comp. Change
Long-Term Historical Population				
Coconino County	1980-2004	75.4	122.1	2.0 %
Flagstaff, AZ-UT MSA	1980-2004	79.4	128.6	2.0
State of Arizona	1980-2004	2,735.8	5,335.8	2.8
United States	1980-2004	227,225.6	285,080.3	0.9
Short-Term Historical Population				
Coconino County	1990-2004	97.1	122.1	1.7
Flagstaff, AZ-UT MSA	1990-2004	102.2	128.6	1.7
State of Arizona	1990-2004	3,679.1	5,335.8	2.7
United States	1990-2004	249,464.7	285,080.3	1.0
Projected Population				
Coconino County	2004-2010	122.1	131.2	1.2
Flagstaff, AZ-UT MSA	2004-2010	128.6	138.3	1.2
State of Arizona	2004-2010	5,335.8	5,998.4	2.0
United States	2004-2010	285,080.3	299,644.5	0.8

**Data points are in 000's.*

Source: Woods & Poole Economics, Inc.

According to Woods & Poole, the population of the Flagstaff metropolitan area increased substantially, by 2.0 percent annually, between 1980 and 2004. During the same period the population throughout the State of Arizona increased even more rapidly, by 2.8 percent annually. By comparison, the population throughout the nation increased by 0.9 percent annually during this period.

Projections indicate that the population of the Flagstaff MSA is expected to increase by 1.2 percent annually throughout the rest of this decade. The State population is expected to increase by 2.0 percent annually through 2010. Forecasts for the United States indicate an average annual compounded population increase of 0.8 percent between 2004 and 2010.

Retail sales levels reflect population trends and the propensity to spend money on retail goods. In markets with substantial retail center developments and other retail destinations, sales levels can reflect the degree to which the surrounding communities rely on the subject community as a hub for retail shopping and other commercial activities. In some markets, such as Flagstaff, sales levels can also reflect the commercial

success of the tourism industry. In areas where tourism or surrounding secondary markets are a significant economic factor, retail sales also reflect the size of the visitor market.

Retail sales figures also reflect one of the largest potential tax bases for local and state governments. Sales tax revenues derive from a broad base of economic activity. Therefore, this can be a relatively stable source of state and local government revenues.

Although there is no direct correlation between retail sales and conference event demand, retail sales trends can provide insight into the economic health and vitality of the subject market. Retail sales growth can indicate prosperity among local businesses. Consistent sales growth can also make a market attractive to new commercial enterprises seeking to enter the market. These factors can lead to increases in the demand for local corporate and consumer events and the supply of retail and entertainment establishments.

Table 4-7 shows historical and projected retail sales data for the Flagstaff MSA and Coconino County. For comparison purposes, HVS also shows figures for the State of Arizona and the United States.

Table 4-7
Retail Sales Trends Data

Data Type	Period	Data Point	Data Point	Avg. Annual Comp. Change
Long-Term Historical Retail Sales				
Coconino County	1980-2004	660.5	1,402.0	3.2 %
Flagstaff, AZ-UT MSA	1980-2004	687.7	1,447.5	3.1
State of Arizona	1980-2004	21,663.6	59,600.8	4.3
United States	1980-2004	1,733,908.9	3,071,531.1	2.4
Short-Term Historical Retail Sales				
Coconino County	1990-2004	907.4	1,402.0	3.2
Flagstaff, AZ-UT MSA	1990-2004	936.7	1,447.5	3.2
State of Arizona	1990-2004	31,712.9	59,600.8	4.6
United States	1990-2004	2,089,724.5	3,071,531.1	2.8
Projected Retail Sales				
Coconino County	2004-2010	1,402.0	1,586.1	2.1
Flagstaff, AZ-UT MSA	2004-2010	1,447.5	1,637.6	2.1
State of Arizona	2004-2010	59,600.8	70,496.3	2.8
United States	2004-2010	3,071,531.1	3,399,787.9	1.7
Long-Term Historical Retail Sales Per Capita				
Coconino County	1980-2004	8,762.3	11,484.4	1.1
Flagstaff, AZ-UT MSA	1980-2004	8,659.0	11,253.5	1.1
State of Arizona	1980-2004	7,918.4	11,169.9	1.4
United States	1980-2004	7,630.8	10,774.3	1.4
Short-Term Historical Retail Sales Per Capita				
Coconino County	1990-2004	9,347.9	11,484.4	1.5
Flagstaff, AZ-UT MSA	1990-2004	9,161.6	11,253.5	1.5
State of Arizona	1990-2004	8,619.9	11,169.9	1.9
United States	1990-2004	8,376.8	10,774.3	1.8
Projected Personal Retail Sales Per Capita				
Coconino County	2004-2010	11,484.4	12,085.3	0.9
Flagstaff, AZ-UT MSA	2004-2010	11,253.5	11,841.5	0.9
State of Arizona	2004-2010	11,169.9	11,752.4	0.9
United States	2004-2010	10,774.3	11,346.1	0.9

**Data points are in 000,000's, except per capita figures.*

Source: Woods & Poole Economics, Inc.

Information from Woods & Poole reveals that between 1980 and 2004, retail sales in the Flagstaff MSA increased at an inflation-adjusted average annual compounded rate of approximately 3.1 percent, compared to a national rate of 2.4 percent. Statewide retail sales grew at an annual rate of 4.3 percent. From 1990 to 2004, retail sales growth in the Flagstaff area increased at a rate of 3.2 percent, compared to a national rate of 2.8 percent. Sales grew at an annual rate of 4.6 percent throughout the State of Arizona.

Retail sales growth is expected to slow somewhat from the pace set in the 1990's. Projections for 2004 to 2010 indicate a growth rate of 2.1 percent in the Flagstaff MSA. The projections call for 2.8 percent annual growth state wide and 1.7 percent nationally during this period.

During the past two decades, retail sales have increased faster in other parts of Arizona than in Flagstaff and Coconino County. However, retail sales growth in Flagstaff has outpaced national growth in retail sales, primarily due to rapid population growth in the local area. Moreover, expansion of the Flagstaff Mall and a proposed Auto Mall may generate substantial growth in local retail sales. Per capita retail sales are currently greater in Flagstaff and Coconino County than they are in Arizona and the United States as a whole.

The sale of food and beverages away from home are roughly equivalent to restaurant and catering sales in a community. Food and beverage sales represent a substantial portion of the service economy. In communities with an active tourism market, food and beverage sales can be a very important segment of the local economy and an important source of state and local tax revenues.

Table 4-8 shows historical and projected restaurant sales data for the Flagstaff MSA and Coconino County. For comparison purposes, HVS also shows sales data for the State of Arizona and the United States.

Table 4-8
Restaurant/Catering Sales Trends Data

Data Type	Period	Data Point	Data Point	Avg. Annual Comp. Change
Long-Term Historical Eating and Drinking Place Sales				
Coconino County	1980-2004	94.1	199.3	3.2 %
Flagstaff, AZ-UT MSA	1980-2004	98.0	205.4	3.1
State of Arizona	1980-2004	2,175.8	5,858.9	4.2
United States	1980-2004	163,115.8	304,369.5	2.6
Short-Term Historical Eating and Drinking Place Sales				
Coconino County	1990-2004	140.0	199.3	2.6
Flagstaff, AZ-UT MSA	1990-2004	143.8	205.4	2.6
State of Arizona	1990-2004	3,303.7	5,858.9	4.2
United States	1990-2004	216,297.9	304,369.5	2.5
Projected Eating and Drinking Place Sales				
Coconino County	2004-2010	199.3	233.5	2.7
Flagstaff, AZ-UT MSA	2004-2010	205.4	240.7	2.7
State of Arizona	2004-2010	5,858.9	7,175.8	3.4
United States	2004-2010	304,369.5	348,529.1	2.3
Long-Term Historical Eating and Drinking Place Sales Per Capita				
Coconino County	1980-2004	1,248.4	1,632.4	1.1
Flagstaff, AZ-UT MSA	1980-2004	1,234.1	1,596.7	1.1
State of Arizona	1980-2004	795.3	1,098.0	1.4
United States	1980-2004	717.9	1,067.7	1.7
Short-Term Historical Eating and Drinking Place Sales Per Capita				
Coconino County	1990-2004	1,442.3	1,632.4	0.9
Flagstaff, AZ-UT MSA	1990-2004	1,406.3	1,596.7	0.9
State of Arizona	1990-2004	898.0	1,098.0	1.4
United States	1990-2004	867.0	1,067.7	1.5
Projected Eating and Drinking Place Sales Per Capita				
Coconino County	2004-2010	1,632.4	1,779.0	1.4
Flagstaff, AZ-UT MSA	2004-2010	1,596.7	1,740.6	1.4
State of Arizona	2004-2010	1,098.0	1,196.3	1.4
United States	2004-2010	1,067.7	1,163.1	1.4

**Data points are in 000,000's, except per capita figures.*

Source: Woods & Poole Economics, Inc.

Since 1980 restaurant sales have increased by about 3.1 percent annually in the Flagstaff MSA. Statewide sales have increased by 4.2 percent annually during this period. The growth rate nationally was 2.6 percent. Since 1990 sales growth has slowed only somewhat in Flagstaff and Arizona to 2.6 percent and 4.2 percent respectively. Restaurant sales are expected to grow by 2.7 percent annually throughout the rest of the decade in Flagstaff and Coconino County. Sales are expected to grow at an annually rate of 3.4

percent throughout the State during this period. Both of these growth rates are faster than the projected national average of 2.3 percent. Rapid population growth and relatively high per capita spending in this category have led to significant growth in food and beverage sales in Flagstaff and throughout Arizona.

Trends in per capita restaurant/catering sales reflect relative spending habits of local residents. Figures also indicate the strength and type of tourism activities in a community. Sales at eating and drinking places also may reflect the quality and quantity of restaurant supply in the market area. Residents of the Flagstaff MSA increased their spending on food away from home by approximately 0.9 percent annually during the past 14 years. The per capita spending on food away from home is significantly higher in Flagstaff and Coconino County than it is statewide and nationwide. This provides some evidence for assessing the willingness of residents to purchase meals at restaurants and other food service providers. It may also reflect relatively high expectations for food quality and service.

Personal income levels are one of the most important indicators of a community's economic health. Trends in per capita personal income reflect the relative spending capacity of area residents, and provide another benchmark for assessing the region's ability to develop and maintain both public and private services and attractions that help make an area an attractive place to live and to visit.

Table 4-9 shows historical and projected personal income trends for Flagstaff and Coconino County. For comparison purposes, HVS also shows income statistics for the State of Arizona and the United States.

Table 4-9
Personal Income Trends Data

Data Type	Period	Data Point	Data Point	Avg. Annual Comp. Change
Long-Term Historical Personal Income				
Coconino County	1980-2004	1,068.0	2,607.1	3.8 %
Flagstaff, AZ-UT MSA	1980-2004	1,120.1	2,753.9	3.8
State of Arizona	1980-2004	47,554.0	136,962.7	4.5
United States	1980-2004	4,191,050.7	8,198,626.1	2.8
Short-Term Historical Personal Income				
Coconino County	1990-2004	1,592.1	2,607.1	3.6
Flagstaff, AZ-UT MSA	1990-2004	1,672.3	2,753.9	3.6
State of Arizona	1990-2004	73,945.1	136,962.7	4.5
United States	1990-2004	5,705,389.4	8,198,626.1	2.6
Projected Personal Income				
Coconino County	2004-2010	2,607.1	3,041.1	2.6
Flagstaff, AZ-UT MSA	2004-2010	2,753.9	3,215.4	2.6
State of Arizona	2004-2010	136,962.7	166,866.5	3.3
United States	2004-2010	8,198,626.1	9,267,194.7	2.1
Long-Term Personal Income per Capita				
Coconino County	1980-2004	14,168.0	21,356.0	1.7
Flagstaff, AZ-UT MSA	1980-2004	14,102.0	21,410.0	1.8
State of Arizona	1980-2004	17,382.0	25,668.0	1.6
United States	1980-2004	18,444.0	28,759.0	1.9
Short-Term Historical Personal Income per Capita				
Coconino County	1990-2004	16,401.0	21,356.0	1.9
Flagstaff, AZ-UT MSA	1990-2004	16,356.0	21,410.0	1.9
State of Arizona	1990-2004	20,099.0	25,668.0	1.8
United States	1990-2004	22,871.0	28,759.0	1.6
Projected Personal Income per Capita				
Coconino County	2004-2010	21,356.0	23,171.0	1.4
Flagstaff, AZ-UT MSA	2004-2010	21,410.0	23,250.0	1.4
State of Arizona	2004-2010	25,668.0	27,818.0	1.3
United States	2004-2010	28,759.0	30,927.0	1.2

**Data points are in 000,000's, except per capita figures.*

Source: Woods & Poole Economics, Inc.

The average income in Flagstaff is approximately \$21,400 per capita. This is well below statewide and national averages. Per capita incomes are even lower elsewhere in Coconino County.

Aggregate income growth historically has been faster in Arizona than in the nation. But per capita incomes have grown faster nationally than they have

in Arizona. This suggests that relatively fast population growth in Arizona has more than made up for relatively slower per capita income growth.

Woods & Poole reports that per capita income rose at an average annual compounded rate of 1.8 percent in the Flagstaff MSA from 1980 through 2004. In the State of Arizona, per capita income rose by 1.6 percent annually between 1980 and 2004. Nationally, per capita income rose at a comparable annual rate of 1.9 percent during this period.

Per capita income growth trends changed in the 1990's. For example, per capita income growth in the Flagstaff MSA was 1.9 percent compared to 1.8 percent throughout the State of Arizona and 1.6 percent nationally. Per capita personal incomes are now growing faster in Flagstaff than they are statewide and nationally.

The projections above indicate that per capita income growth will slow somewhat in the coming decade. Income per capita is expected to grow at an annual rate of 1.4 percent in the Flagstaff MSA and Coconino County. Per capita income is projected to grow at an annual rate of 1.3 percent in Arizona throughout the rest of the decade. Per capita personal income across the nation is expected to grow at an annual rate of 1.2 percent between 2004 and 2010.

Labor Market Characteristics

During the past decade Flagstaff's labor market has demonstrated a relatively high rate of unemployment compared to the state and nation. During the past three years, however, Flagstaff's unemployment rate has remained relatively low compared to the state and nation. Some continued slack in the labor market reflects a growing dependence on the trade and service sectors of the economy, including tourism. A large number of government jobs also add stability to the labor market.

Table 4-10 shows employment statistics for the City of Flagstaff. For comparison purposes, HVS also shows annual unemployment rate data for Coconino County, the State of Arizona, and the United States.

Table 4-10
Flagstaff Labor Market Data

Year	City of Flagstaff				Coconino County % Unemployed	Arizona % Unemployed	U.S. % Unemployed
	Labor Force	Total Employment	Total Unemployment	% Unemployed			
1990	26,111	24,507	1,604	6.1	7.8	5.5	5.6
1991	26,415	24,886	1,529	5.8	7.3	5.8	6.8
1992	28,009	25,923	2,086	7.4	9.4	7.6	7.5
1993	28,358	26,406	1,952	6.9	8.7	6.3	6.9
1994	31,218	28,935	2,283	7.3	9.2	6.4	6.1
1995	33,185	31,152	2,033	6.1	7.8	5.1	5.6
1996	31,861	29,668	2,193	6.9	8.7	5.5	5.4
1997	31,399	29,317	2,082	6.6	8.4	4.6	4.9
1998	32,107	30,255	1,852	5.8	7.3	4.1	4.5
1999	33,911	32,117	1,794	5.3	6.7	4.4	4.2
2000	34,459	32,882	1,577	4.6	5.8	4.0	4.0
2001	35,324	33,817	1,507	4.3	5.4	4.7	4.7
2002	36,250	34,588	1,662	4.6	5.8	6.2	5.8
2003	35,470	33,672	1,798	5.1	6.4	5.6	6.0
Average	31,720	29,866	1,854	5.9	7.5	5.4	5.6

Sources: U.S. Bureau of Labor Statistics, Arizona Department of Economic Security

Flagstaff's labor force peaked in 2002 with approximately 36,250 potential workers. Employment also peaked in 2002, with approximately 34,600 workers. As the national and regional economies entered a recession in 2001, the labor force and employment continued to grow in Flagstaff. A decline in the local labor force and employment did not occur until 2002 and 2003, reflecting a lag behind national trends.

The average annual unemployment rate in Flagstaff increased from 4.3 percent in 2001 to 5.1 percent in 2003. Unemployment rates in the City of Flagstaff are somewhat lower than unemployment rates throughout Coconino County and the State of Arizona. Some preliminary economic data suggests the regional economy has resumed growth in 2004. But it is unclear whether a recovery has begun in the labor market.

The proposed hotel conference center would employ several dozen local area employees. But it would represent a small portion of the overall labor force. The relatively slack labor market suggests that it will not be difficult to find qualified and affordable employees for the subject facility. HVS

interviews with existing hotel property managers in Flagstaff generally confirmed this view.

County employment trends are a good source of data for understanding the broader local labor market in the Flagstaff MSA and Coconino County. As the primary population center in northern Arizona, Coconino County offers the most developed labor market in this part of the state.

Table 4-11 shows employment trends by industry sector in Coconino County.

Table 4-11
Employment by Sector for Coconino County

											Average Annual Compounded Percent Change					
	1980	Percent of Total		1990	Percent of Total		2004	Percent of Total		2010	Percent of Total		1980- 2004	1990- 2004	2004- 2010	
Industry																
Farm	0.3	0.8 %		0.3	0.6 %		0.2	0.3 %		0.2	0.3 %		(0.6) %	(1.7) %	(0.5) %	
Agriculture Services, Other	0.1	0.4		0.2	0.5		0.6	0.9		0.7	0.9		6.2	7.0	2.4	
Mining	0.1	0.2		0.2	0.3		0.2	0.2		0.2	0.2		4.2	0.2	(0.1)	
Construction	2.0	5.8		2.4	4.8		3.7	5.2		3.8	4.8		2.5	3.3	0.5	
Manufacturing	2.6	7.3		3.6	7.3		3.5	4.9		3.6	4.6		1.3	(0.1)	0.5	
Trans., Comm. & Public Utils.	2.2	6.2		2.0	4.1		2.1	3.0		2.2	2.8		(0.1)	0.6	0.4	
Total Trade	7.6	21.6		11.7	23.8		17.6	24.6		19.7	24.8		3.5	3.0	1.9	
Wholesale Trade	0.5	1.4		0.8	1.6		1.5	2.1		1.7	2.1		4.9	4.7	1.5	
Retail Trade	7.1	20.2		10.9	22.2		16.1	22.5		18.0	22.8		3.4	2.8	1.9	
Finance, Insurance, & Real Estate	2.1	5.9		2.1	4.2		4.0	5.6		4.5	5.7		2.8	4.9	2.1	
Services	9.1	25.8		15.0	30.5		23.9	33.5		27.6	34.8		4.1	3.4	2.4	
Total Government	9.2	26.1		11.7	23.8		15.5	21.7		16.7	21.0		2.2	2.0	1.3	
Federal Civilian Govt.	3.3	9.4		3.1	6.2		2.6	3.7		2.5	3.1		(1.0)	(1.1)	(0.9)	
Federal Military Govt.	0.2	0.7		0.4	0.8		0.3	0.4		0.3	0.4		0.9	(1.7)	(0.1)	
State & Local Govt.	5.6	16.0		8.2	16.8		12.5	17.6		13.9	17.5		3.4	3.0	1.7	
TOTAL	35.3	100.0 %		49.0	100.0 %		71.3	100.0 %		79.2	100.0 %		3.0 %	2.7 %	1.8 %	

*Figures are in 000's, except percentages.

Source: Woods and Poole Economics, Inc.

Total employment in Coconino County has increased from about 35,300 employees in 1980 to approximately 71,300 employees in 2004. Tracking national trends, rapid employment growth has occurred in the trade and service sectors. State and local government employment has also increased substantially as the population and local economy have grown.

The labor market in Coconino County depends heavily on trade, service, and government jobs. These three sectors represent approximately 80 percent of labor market. Construction jobs have increased significantly during the past two decades. But this sector still only represents about 5.2 percent of overall employment. Manufacturing increased somewhat in the 1980's, but declined again in the past few years. Retail trade has grown rapidly from about 7,100 employees in 1980 to about 16,100 employees in 2004. Similarly, the service sector had roughly 9,100 employees in 1980 compared to 23,900 employees in 2004. State and local government supply jobs for about 12,500 employees.

Projected Economic Growth

Table 4-12 shows projections of growth in total real (inflation-adjusted) earnings by the major sectors of the economy in Coconino County. These projections are presented in constant 1992 dollars, as reported by the Bureau of Economic Analysis.

Table 4-12
Earnings by Industry Sector Coconino County

Industry Sector	1980	1990	2004	2010	Projected Annual Change
Farm	8.335	2.841	3.903	3.729	-0.8%
Agriculture Services, Other	1.480	3.067	7.674	9.347	3.3%
Mining	3.909	5.899	7.596	7.618	0.0%
Construction	79.013	62.427	103.754	111.073	1.1%
Manufacturing	73.920	97.417	128.215	144.641	2.0%
Trans., Comm. & Public Utils.	89.424	65.831	77.245	83.870	1.4%
Wholesale Trade	13.802	23.214	40.790	45.770	1.9%
Retail Trade	109.366	144.313	237.356	275.804	2.5%
Finance, Insurance, & Real Estate	18.897	24.800	82.872	103.621	3.8%
Services	158.590	278.852	540.436	684.319	4.0%
Federal Civilian Govt.	129.869	128.467	141.728	140.505	-0.1%
Federal Military Govt.	2.217	5.162	4.788	5.023	0.8%
State & Local Govt.	151.479	271.429	411.544	479.023	2.6%
Total Earnings*	840.301	1,113.719	1,787.901	2,094.343	2.7%

*Earnings are in Millions 1992 constant dollars.

Sources: Bureau of Economic Analysis, Woods & Poole Economics, Inc.

Economic growth, as measured by total earnings, is expected to grow fastest in the services, by an annual rate of 4.0 percent throughout the rest of this decade. Earnings in finance, insurance and real estate services are also expected to grow quickly, at an annual rate of nearly 3.8 percent through

2010. Though only a small fraction of the labor market, employment in agricultural services is expected to increase by 3.3 percent during this decade. State and local government, retail trade, and wholesale trade are declined in expected to grow significantly as well. A 2.0 percent increase in manufacturing employment may occur due to a broad economic recovery expected nationally in the next few years. Annual earnings growth in the construction, transportation, and federal government sectors are projected to increase at slower rates throughout the rest of the decade.

Transportation

Flagstaff has a well developed arterial street and highway system, including Route 66, Interstate 40, and Interstate 17. The primary arterial street through Flagstaff is Route 66, along which much of the area's commercial businesses and tourism services are located. Interstate 40 connects Flagstaff to Albuquerque in the east and Los Angeles to the west. Interstate 17 connects Flagstaff to Phoenix in the south. Highway 89 connects Flagstaff to St. George, Utah to the north and Prescott to the south. Highways 64 and 180 connect Flagstaff to the Grand Canyon to the north.

Several transportation options are available to Flagstaff visitors and residents for air, rail, bus, and automobile travel. HVS reviewed various transportation service companies listed on switchboard.com and in documents provided by the Flagstaff Convention & Visitors' Bureau.

Table 4-13 identifies these transportation service companies and public transit operations that serve the Flagstaff area.

Table 4-13

Transportation Companies and Services in Flagstaff Area

Auto Rental	Air Travel
Avis Rent-A-Car	Phoenix Sunport
Enterprise Rent-A-Car	Flagstaff Pulliam Airport
Hertz	Grand Canyon Nat'l Park Airport
National Car Rental	Taxi & Limo Services
X-Press Rent-A-Car	A-1 Quick Cab
Recreational Vehicle Rental	A Deluxe Taxi
Advantage	A Friendly Cab
Cruise America	Arizona Taxi & Tours
Luxury Travel Service	Mountain Cab
Trains & Cargo	Sun Taxi & Tours
Amtrak	Wiseman Aviation & Limo
Arizona Specialty Courier	Yellow Cab
Greyhound Package Express	Bus Lines
Public Transportation	American Dream Tours
Coconino Yavapai Shuttle	Open Road Tours
Mountain Line	Greyhound Bus Lines

Sources: Flagstaff CVB, switchboard.com

Flagstaff is primarily a drive-in destination and pass-through market for tourists. Two main visitor seasons attract travelers to the area. In the summer, large numbers of out-of-town tourists travel through Flagstaff on their way to the Grand Canyon. In-state visitors from southern Arizona visit Flagstaff to enjoy its mild summer climate. In the winter, large numbers of in-state and regional visitors travel to Flagstaff for skiing and other winter recreational activities.

Table 4-14 shows annual average daily traffic counts along the major highways and interstates that serve the Flagstaff market area.

Table 4-14

Annual Average Daily Traffic Counts

Traffic Route	Exit Number	1980	1990	2000	2002	CAGR*
I-40	Exit 201	7,700	14,000	19,087	18,417	4.0%
I-17	Exit 337	11,000	19,000	33,181	34,794	5.4%
Route 66	Exit 53	17,000	13,000	16,333	16,720	-0.1%
Highway 89	S.R. 64	5,800	4,600	6,101	6,464	0.5%
Highway 64	U.S. 180	2,171	3,300	4,966	4,333	3.2%

*Compound annual growth rate between 1980 and 2002.

Source: Arizona Department of Transportation

Vehicle traffic on I-17 and I-40 has increased rapidly during the past two decades. Transportation officials attribute this to substantial population growth throughout the state and a continued boom in the housing market. State Highway 66 also experienced increased volumes of traffic during the past two decades. Traffic along Route 66 declined in the 1980's. But it rebounded significantly in the 1990's along this route. Traffic counts along U.S. Highway 89 have remained relatively stable during the past two decades. As the primary entry and exit for the Grand Canyon, approximately 2.4 million vehicles in 2002 traveled along this highway in 2002.

In addition to vehicle traffic, there are three airports that serve Flagstaff residents and visitors to the area. The Phoenix Sky Harbor International Airport is the only major international airport in the State of Arizona. The Pulliam Airport is Flagstaff's regional airport. America West is the primary commercial airline that operates at the Pulliam Airport. The Grand Canyon National Park Airport supports a small number of private and commercial airlines.

Table 4-15 shows airport passenger utilization data during the past ten years for the three airports considered in this study.

Table 4-15

Total Annual Enplanement Estimates at Selected Airports

Year	Phoenix Sky Harbor Int'l Airport	% Chg	Flagstaff Pulliam Airport	% Chg	Grand Canyon Nat'l Park Airport	% Chg
1987	8,561,523	-	41,463	-	N/A	-
1988	9,589,050	12.0%	47,006	13.4%	N/A	-
1989	10,357,030	8.0%	51,891	10.4%	N/A	-
1990	10,859,034	4.8%	51,687	-0.4%	N/A	-
1991	11,070,219	1.9%	48,304	-6.5%	N/A	-
1992	11,059,200	-0.1%	49,508	2.5%	N/A	-
1993	11,810,891	6.8%	42,262	-14.6%	N/A	-
1994	12,813,066	8.5%	41,138	-2.7%	N/A	-
1995	13,928,098	8.7%	39,213	-4.7%	N/A	-
1996	15,205,926	9.2%	47,171	20.3%	N/A	-
1997	15,404,953	1.3%	47,059	-0.2%	N/A	-
1998	15,984,620	3.8%	39,573	-15.9%	654,020	-
1999	16,507,680	3.3%	38,530	-2.6%	617,360	-5.6%
2000	17,601,558	6.6%	36,463	-5.4%	563,574	-8.7%
2001	17,568,865	-0.2%	33,371	-8.5%	414,138	-26.5%
2002	17,613,420	0.3%	38,455	15.2%	330,980	-20.1%
2003	18,598,477	5.6%	36,407	-5.3%	344,289	4.0%

Sources: HVS interviews with individual airport managers.

Phoenix Sky Harbor is by far the busiest airport in Arizona. This international airport had more than 18 million enplanements in 2003, as estimated by the Phoenix Department of Aviation. Total enplanements have increased substantially during the past 15 years. The only two years in which enplanements declined were 1992 and 2001, consistent with national trends. Geopolitical concerns and national economic recessions led to less corporate and leisure travel in Phoenix during both of these periods. This is consistent with national trends. Although 2003 estimates are preliminary, based on 11 months of data, it appears that significant growth occurred in 2003.

Enplanements at the Grand Canyon National Park Airport have declined substantially in four of the past five years. An international economic recession and reduced travel budgets for households and corporations may have placed substantial downward pressure on demand for this airport serving the Grand Canyon. Enplanements dropped to their lowest level in 2002. Furthermore, the number of airlines serving this airport declined from 23 companies to 16 companies between 1999 and 2002. A rebound occurred

in 2003, suggesting stabilization or resumed growth for the airport. A significant number of enplanements arrive at the Grand Canyon from the Las Vegas market. Currently Air Grand Casino and Air Vegas account for approximately 14 percent of all enplanements.

The most direct air service to Flagstaff is via the Pulliam Airport, owned by the City of Flagstaff. Currently America West Express is the only commercial airline serving Flagstaff. Through 1994 Sky West also had flights into Pulliam Airport. Individuals and corporations owning small airplanes may use the 6,999 foot asphalt runway at the Pulliam Airport. Approximately 132 private aircraft are based at the airport. Only about 11 percent of the aircraft operations at Pulliam Airport are commercial flights.

The City plans to expand air service to Flagstaff by extending the Pulliam Airport runway by approximately 1,800 feet. Several key factors, including federal funding and environmental assessments, will determine the timetable for the proposed expansion project. The environmental assessment is scheduled to be completed in 2005. Design work could be completed as soon as 2006. The City anticipates construction will be completed in 2007. A successful expansion of the Pulliam Airport would allow for the use of regional jets and could partially mitigate the perception that access to Flagstaff is difficult for certain groups.

Climate

Flagstaff's combination of altitude, low humidity, and terrain provide mild weather conditions and clear air throughout the year. Flagstaff is considered high desert region. The city is surrounded by a forest of Ponderosa Pine trees at an altitude of 7,000 feet above sea level. Therefore, average temperatures are much cooler in Flagstaff than in other parts of Arizona, such as Phoenix.

Table 4-16 shows the average daily temperature, by month, in Flagstaff compared to Phoenix.

Table 4-16

Month	Flagstaff		Phoenix	
	High	Low	High	Low
January	42	15	68	39
February	45	18	71	43
March	49	21	77	48
April	58	27	84	54
May	67	33	93	62
June	78	41	101	68
July	82	51	104	76
August	79	49	103	77
September	73	41	99	70
October	63	31	88	57
November	51	22	76	45
December	43	16	67	38

Sources: Flagstaff CVB, WeatherSmith

Temperatures are much cooler in Flagstaff than in Phoenix, especially during the very hot months of June, July, August, and September when high temperatures in Phoenix are near or above 100 degrees.

According to information from the Flagstaff Convention & Visitors' Bureau, there are, on average, 288 days of sunshine each year in Flagstaff. Annual precipitation is 22.8 inches or 57 centimeters. Annual snowfall is approximately 108.8 inches or 272 centimeters. The mild climate in the summer makes Flagstaff a comfortable getaway location for many Arizona residents who live in Phoenix or other southern parts of the state. Cold temperatures and snowfall in the winter make Flagstaff one of the region's only skiing destinations.

Market Area Implications

A growing population, moderate summer climate, affordable labor rates, and other demographic characteristics make Flagstaff an attractive market for residential and commercial growth. Moreover, the weather, proximity to the Grand Canyon, and abundant recreational opportunities make Flagstaff an attractive visitor market. The community's rapid residential growth for permanent residents as well as second homes testifies to the community's positive image.

The local economy has a modest base of corporate and household income that could generate demand for local meetings and banquet space. But the proposed facility will need to target out-of-town groups to generate

additional conference demand to produce high utilization rates for an upscale conference center.

Flagstaff's tourism infrastructure is limited compared to larger urban convention destinations. The supply of upscale, full-service hotels is currently limited to three properties, which offer a total of 550 guestrooms. Highway transportation access is excellent. Interstate 17 provides efficient access to the growing Phoenix metropolitan market and other parts Arizona. But air transportation is limited and inconvenient. Major historic and cultural amenities such as Route 66, the Grand Canyon, and Flagstaff's historic downtown district continue to attract large number of out-of-town visitors. But there is a very limited supply of upscale meeting and conference space in the community. Established visitor destinations such as the Arizona Snow Bowl and the Grand Canyon attract several million out-of-town guest visits annually. Currently, much of Flagstaff's visitor market consists of independent leisure travelers. HVS discusses visitor segments in greater detail later in this report.

The proposed hotel conference center would allow Flagstaff to broaden its visitor base to include more meetings and group business. The proposed facility would provide a competitive advantage that most communities of this size do not have. However, the substantial supply of lower priced guest rooms in the market will create downward pressure on room rates. As with other projects that significantly change the make-up of hotel and meeting room supply, aggressive marketing efforts will be required initially to inform potential user groups of the facility and to attract a targeted base of out-of-town group business.

Although per capita incomes are relatively low in Flagstaff, sustained increases in earnings and employment reflect the overall health of the local economy. The region has enjoyed relative economic stability due to the strong presence of government and trade as well as growth in finance, insurance, and real estate services. As a whole, the subject market has experienced rapid growth in the service sector, consistent with national trends.

Locally, a small number of major employers in manufacturing, health care, education, and government have provided a degree of economic security for

Flagstaff. But the local economy continues to produce unemployment rates above four percent, indicating significant slack remains in the labor market.

The effectiveness of the proposed facility to generate economic impacts for the entire community will depend on Flagstaff's ability to attract statewide and regional meetings and small conventions. The financial feasibility of the proposed facility may depend more on its ability to book upscale local events in the meeting and banquet space when out-of-town groups are not using the facility. Moreover, the proposed facility's financial feasibility is likely to be contingent on its ability to sustain average daily room rates by targeting corporate and group business for its guest rooms.

HVS discusses demand potential for upscale conference space and hotel rooms throughout in this report. Our analysis will estimate the demand potential for events, and evaluate the feasibility of developing the proposed hotel conference center. This evaluation will be based both on the project's financial feasibility and its ability to generate economic impacts for the community at large. Before evaluating demand potential, however, the following sections will review the competitive supply and comparable facilities in other markets.

5. Conference Center Industry Trends

The purpose of this section is to describe the conference center and meeting industry and analyze trends in events and attendance at meetings and conferences. HVS also reviews key site selection criteria that meeting planners identify as the most important factors in determining where to hold their events. The definitions provided herein will augment the market analysis. The overview of industry trends will aid in assessing the demand potential for a conference center in Flagstaff. This section concludes with an assessment of the particular implications of these trends for the development of a new hotel conference center in Flagstaff.

Industry Overview

The conference center market is a specialized segment of the hospitality industry. During the early 1960s, large corporations began purchasing off-premises buildings (often old mansions) and converting them into meeting and retreat grounds for upper-level executives. Because these early conference centers were dedicated to the use of one corporation, their popularity was limited and the general public had little knowledge of their existence. During the 1980s, professional operators entered the field. Today, true conference centers are able to circumvent the problems associated with holding meetings at traditional hotels by offering a self-contained meeting, learning, and living environment, thereby minimizing the loss of momentum caused by evening adjournments.

Conference centers are defined by the International Association of Conference Centers (“IACC”) as facilities with the primary purpose of accommodating small- to medium-sized meetings by offering a self-contained, full-service meeting environment. Conference centers often provide on-site recreational amenities such as golf and tennis, which serve to facilitate group activities and discourage outside distractions. The International Association of Conference Centers has a stringent list of universal membership criteria that is reviewed periodically, a copy of which

is available upon request from IACC. Some key priorities of business for IACC facilities are outlined in the following discussion.

- Average group size of 75 people or less;
- A minimum of 60% (based on net area) of meeting space in the conference center must be dedicated, single-purpose conference space;
- A minimum of 60% of total sales must be generated by conferences (if the conference center is ancillary to a resort or convention hotel, a minimum of 70% of total sales of the conference center must be generated by conferences);
- The conference center must offer and promote package plans which include conference rooms, guestrooms, three meals, continuous refreshment service, conference services and basic audiovisual (A/V) services (nonresidential package includes conference rooms, lunch, continuous refreshment service, conference services, and basic A/V);
- The conference center must be staffed with skilled conference planners who can provide customized services that enable the client to meet the objectives of the meeting;
- The conference center must have skilled technicians proficient in providing creative program consultation; equipment setup, operation, and instruction; and immediate response to service needs;
- Guestrooms must include adequate work stations, adequate reading and work lighting, and comfortable seating; and
- The conference center must have separate dining and conference facilities, with at least one dining area available specifically for the convenience of conference groups.

IACC requirements indicate a narrow definition for conference centers. Numerous other conference facilities are located throughout North America. Although they do not meet the specific requirements set by IACC, many of these facilities are high-end properties that host conferences and meetings for corporate, association, and other group clients. Examples include the Monterey Conference Center in California and the Whistler Conference Center in British Columbia.

Types of Conference Centers

The competitive environment is dominated by four types of conference centers: executive, resort, corporate, and educational. HVS discusses these four types of conference centers individually.

Executive Conference Centers

Executive conference centers are designed to meet the needs of mid- to upper-level executive and managerial meetings. These functions may revolve around strategic planning, forecasting and budgeting, sales and marketing, state-of-the-corporation reports, new product introductions, and educational and training seminars. Demand generators include corporations, associations, and institutions. Executive conference centers are designed to minimize external noise, congestion, the lure of off-site activities, and similar distractions.

Large executive conference centers are often characterized by a "think-tank" atmosphere and feature full audiovisual capabilities, recreational opportunities, and first-class amenities. Many smaller facilities cultivate a residential ambiance and resemble mansions, retreats, or park-like estates. The following is a list of regionally and nationally prominent executive conference centers.

- Arbor Day Farm/Lied Conference Center - Nebraska City, Nebraska
- Chattanooga Hotel Conference Center – Chattanooga, Tennessee
- Harrison Conference Center - Glen Cove, New York

Resort Conference Centers

Resort conference centers provide all of the facilities and services available at executive conference centers, but place a greater emphasis on recreational activities in a resort setting. Although small corporate meetings are the main source of business, recreational activities are regularly scheduled, integral components of the program. The recreational opportunities and resort amenities associated with these properties are critical to their success.

In many cases, resort conference centers have a broader target market than executive conference centers. These properties are flexible enough to accommodate both resort guests and meeting attendees. Many meeting

planners welcome the opportunity to provide breaks during intensive meetings by scheduling golf tournaments or other leisure activities. Some companies also use resort conference centers when offering incentive trips for employees and their spouses. Examples of destination conference center resorts include the following:

- Scottsdale Resort & Conference Center - Scottsdale, Arizona
- The Woodlands Conference Center and Resort – The Woodlands, Texas
- Resort at Squaw Creek - Olympic Valley, California
- Inverness Hotel and Golf Club - Englewood, Colorado
- Barton Creek Conference Resort - Austin, Texas
- Cheyenne Mountain Conference Resort - Colorado Springs, Colorado

Corporate Conference Centers

Corporate conference centers are similar to executive conference centers; their distinguishing feature is that they are owned and sometimes operated by a specific corporation and are often located on or near the grounds of a large company facility. Many corporations have made their facilities available to outside users during periods of low demand. A recent trend has been the conversion of in-house conference centers to facilities that are open to public user groups. Although these facilities are open to a broad market of users, they often cater specifically to the company which owns the center.

Corporate conference centers generally give priority to the affiliated company when booking guestrooms and function space. Outside users are viewed as a secondary source of demand that can augment the facility's overall level of business. Efficient accommodation of the needs of the affiliated company is often the primary concern of these conference centers, rather than profitability. Examples of nationally prominent corporate conference centers include the following centers:

- North Maple Inn - Basking Ridge, New Jersey
- Sears Conference and Training Center - Hoffman Estates, Illinois
- Coca-Cola Company Learning Center - Atlanta, Georgia

- IBM Palisades Conference Center - Palisades, New York

Educational Conference Centers

Educational and non-profit conference centers are similar to corporate centers, but are owned and sponsored by colleges, universities, or medical centers. For the most part, these facilities are used to host educational meetings. Examples of educational conference centers include the following:

- Columbia University's Arden House
- Emory Conference Center Hotel
- MIT Endicott House
- Fairfield University's Center for Financial Study

Facility Characteristics

In order to properly accommodate a wide range of events, a conference center facility requires meeting space – divided into both general session space and meeting / breakout spaces – capable of supporting conferences and meetings. Modern conference centers also provide pre-function space suitable for attendee registration as well as light exhibit uses. Kitchen facilities support event catering. Presentation equipment needs to be suitable for both large groups and breakout sessions. In a large conference center, the main ballroom should be divisible in order to support simultaneous events.

- **Main Ballroom** — in conference centers the main ballroom space typically serves as both a large banquet area and a meeting space for general sessions. In some instances this space can be designed for exhibit use as well. If it is used for exhibits the space requires high ceilings and clear spans with limited numbers of support columns in the room. The quality level of this space must be sufficient to be appropriate for formal dinners and social functions. If exhibition events are part of the target market, this space also needs to avoid materials or fixtures that are easily damaged by the level of utilization associated with exhibits. The space should have durable carpeting and appear like a true ballroom rather than an exhibit hall. The space should be divisible with soundproof movable walls. Sound attenuation and sophisticated sound systems are also

important features of a ballroom. Proximity to kitchen facilities is vital for the efficient delivery of food services.

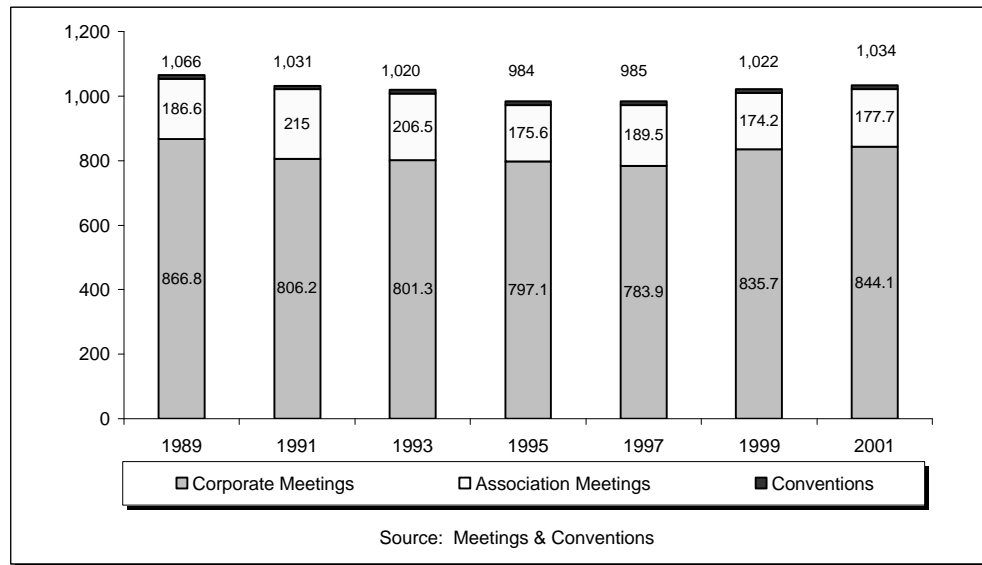
- **Meeting or breakout rooms** — intended for small groups, individual rooms may vary in size from 500 to 2,000 or more square feet. They are often divisible into smaller units to provide maximum flexibility. Meeting rooms are characteristically carpeted and have a high level of finish. Most meeting spaces have flat floors and no fixed seating so that they can be configured for an assortment of meeting styles. Meeting rooms offer variable lighting setups, sound attenuation, and in newer facilities, access to advanced telecommunications technology. Some meeting rooms are designed exclusively for presentations and may have fixed tiered theater style seating and video projection capabilities. Boardrooms are elegant meeting rooms with the permanent installation of a conference table.
- **Pre-function space** — space located just outside of or adjacent to the event space. Pre-function areas support the circulation of pedestrian traffic through the facility, serve as registration areas, and are essential to the control of access to event spaces. Terraces or other signature function spaces can supplement the typical lobby areas.

Number of Meetings

According to the 2002 Meetings & Conventions Meetings Market Report there are more than one million meetings booked in the United States each year by corporations, associations, and convention meeting planners. Meetings & Conventions publishes this report every two years. The 2004 publication will be available later this year, reflecting more recent industry data for the meetings market.

Figure 5-1 shows the total number of meetings held annually in these three specific meeting segments throughout the 12 most recently available years.

Figure 5-1
Total Number of Meetings (in Thousands)



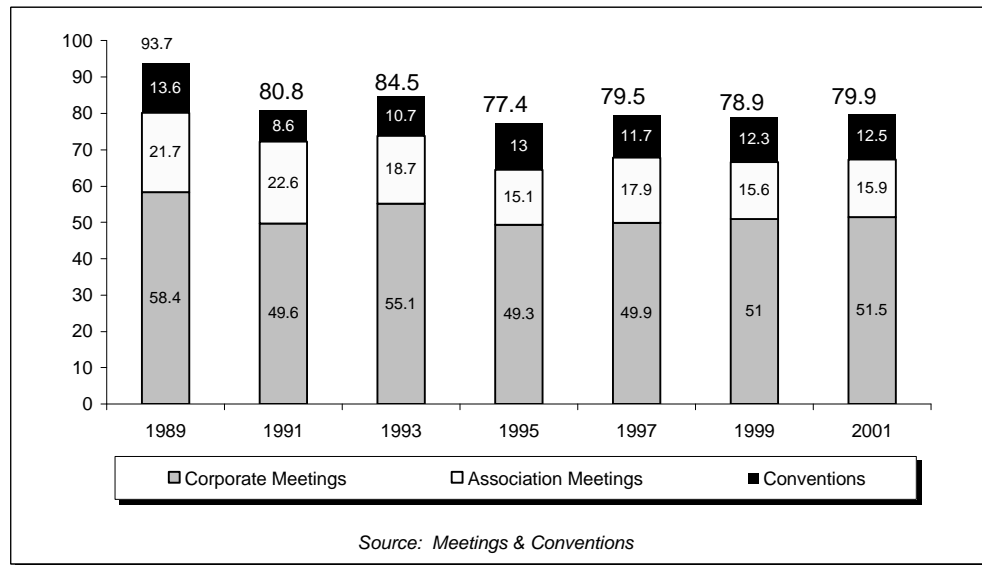
For more than a decade there have been approximately one million meetings and conventions annually in the United States. The majority of these events are corporate meetings. Associations also generate a large number of meetings. For the past twelve years there have been between 10,000 and 12,000 conventions held annually in the United States as well. The total number of meetings and conventions has stayed in a somewhat narrow range during the course of the past 12 years. The number of meetings in 2001 represents a slight increase over 1999, although the year 2000 was presumably a peak year that exceeded both 1999 and 2001 in the total number of events.

Attendance Trends

Approximately 80 million people participate in meetings and conventions each year in the United States, based on the most recent data from Meetings & Conventions.

Figure 5-2 shows total attendance figures for the meeting industry during the past 12 years.

Figure 5-2
Attendance (in millions)



Attendance at meetings has been approximately 80 million people during recent years in the United States. Total attendance in the meetings industry has declined from its peak level in the late 1980s, when annual attendance at meetings exceeded 90 million people. Throughout the 1990s the number of people attending association meetings has generally declined. Over the past half decade the number of people attending corporate meetings has been relatively stable, as with attendance at conventions.

Table 5-1 shows the average meeting size for these three market segments over the past 12 years. The compound annual growth rate (“CAGR”) for each meeting category shows how quickly average attendance increased or decreased over each two-year period on an annual basis.

Table 5-1

Average Meeting Size by Event Type

Type of Event / Growth	1989	1991	1993	1995	1997	1999	2001
Conventions							
Average Attendance	1,079	843	907	1,193	1,035	1,060	1,059
CAGR	--	-11.6%	3.7%	14.7%	-6.8%	1.2%	0.0%
Associations							
Average Attendance	116	105	91	86	94	90	89
CAGR	--	-4.9%	-7.2%	-2.6%	4.8%	-2.6%	0.0%
Corporate Meetings							
Average Attendance	67	62	69	62	64	61	61
CAGR	--	-4.4%	5.7%	-5.2%	1.5%	-2.1%	0.0%

Source: Meetings and Conventions, 2002

As attendance has declined, so has the average meeting size over the past 12 years. Conventions drew an average of 1,059 people in 2001, compared to an average attendance of 1,079 in 1989. This figure is cyclical and can fluctuate with other factors in an economic cycle. Travel costs, transportation safety, changes in technology and communications, and the expected payoff for meetings also have significant effects on attendance. In 1995 convention attendance peaked, when the average convention had 1,193 people in attendance. Association meetings drew an average of 89 people in 2001, compared to 116 in 1989. Attendance at corporate meetings is also somewhat lower than it was in 1989 when the average meeting had 67 people. In 2001 the average corporate meeting had 61 people. In 1993 corporate meeting attendance peaked, when the average meeting attendance was 69 people. These average attendance figures, despite minor fluctuations, have been relatively stable during the past decade.

Facility & Event Characteristics

HVS summarized various industry data related to the size of conference centers, the character of conference center demand, sources of demand, and sources of competition. To supplement our own industry research and survey data, HVS has identified additional information sources that will augment our understanding of the conference center industry. For example, PKF and IACC compiled survey data from conference centers throughout North America for their 2003 Conference Center Industry Trends report. The annual report tracks trends in conference center event bookings, demand, event types and other performance variables for residential conference centers. A secondary source for industry data is the 2002 Compass Report published by Horwath Horizon.

Figure 5-3 presents key facility program data for each of the four types of conference center defined in this section.

Figure 5-3
Residential Conference Center Facility Programs

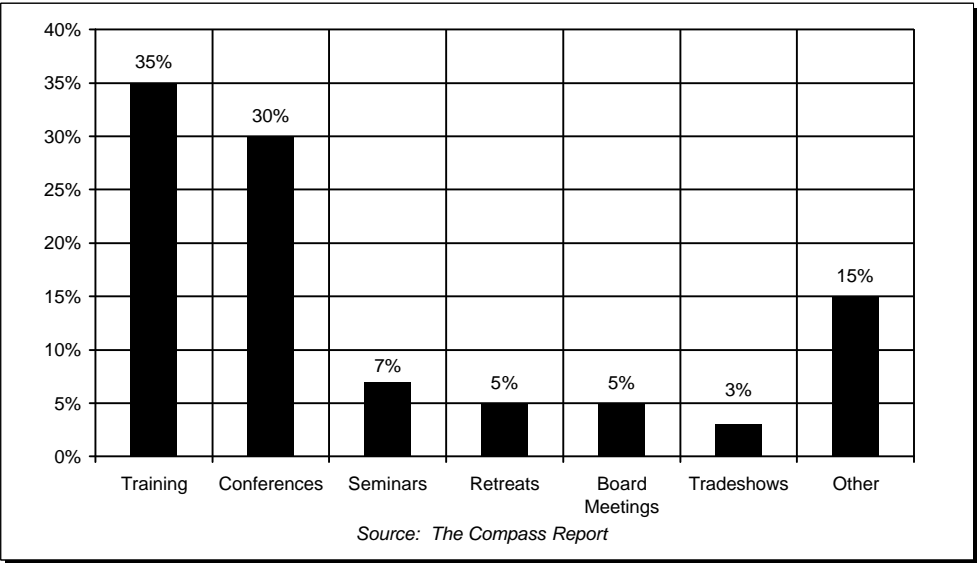
Conference Center Type	# of Guest Rooms	Dining Room Capacity	# of Meeting Rooms	Avg. Meeting Room Size (Sq. Ft.)	Total Meeting Room Space (Sq. Ft.)
Executive	179	227	25	690	17,209
Resort	306	399	28	1,053	29,571
Corporate	248	286	45	823	36,889
Educational	180	320	22	884	19,360

Source: 2003 Conference Center Industry Trends

On average, these conference centers have between 17,000 square feet and 37,000 square feet of meeting space. They have between 179 and 306 guest rooms. They generally have between 22 and 45 meeting rooms. The average size for meeting rooms ranges between 690 square feet at executive conference centers and 1,053 square feet at resort conference centers. Resort conference centers have the most guest rooms and largest dining rooms, on average. But corporate conference centers have the largest number of meeting rooms and the largest amounts of total meeting space.

Figure 5-4 shows the various types of events held in conference centers.

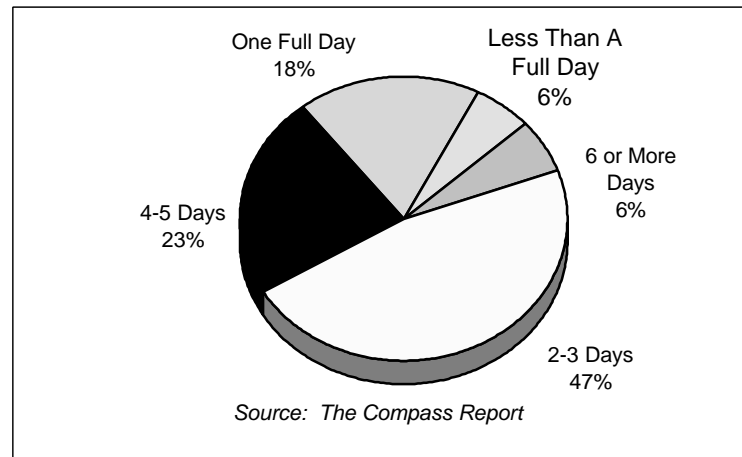
Figure 5-4
Conference Center Events



Training sessions, conferences and seminars are consistent with corporate and educational institution use of conference centers. Tradeshow, which account for five percent of the events at conference centers included in the Compass Report, are more commonly associated with convention centers as those facilities feature more exhibition space than do conference centers.

Figure 5-5 shows the event lengths of the various events booked in the conference centers studied in the Compass Report.

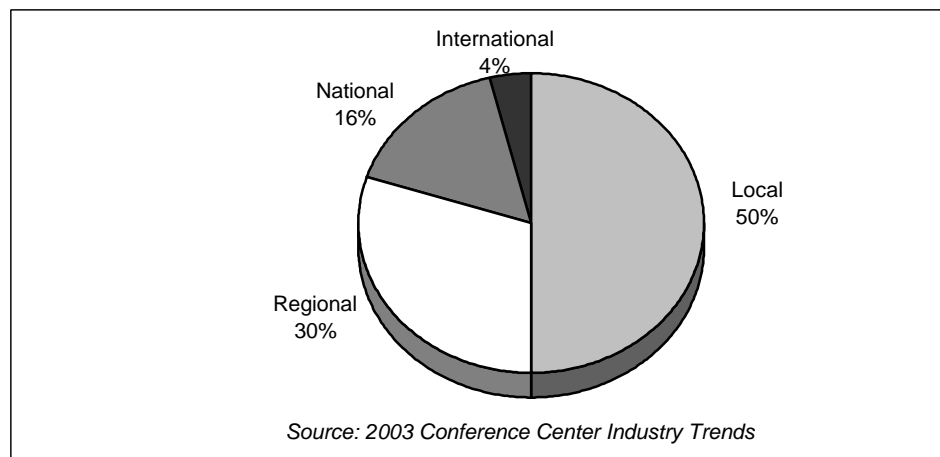
Figure 5-5
Conference Center Event Length



Nearly one-fourth of the events booked in conference centers surveyed in the Compass report were approximately one day or less in length. Nearly half of the events lasted two or three days. Approximately one-fourth of events last four days or longer.

Figure 5-6 shows which demand sources book meetings at conference centers.

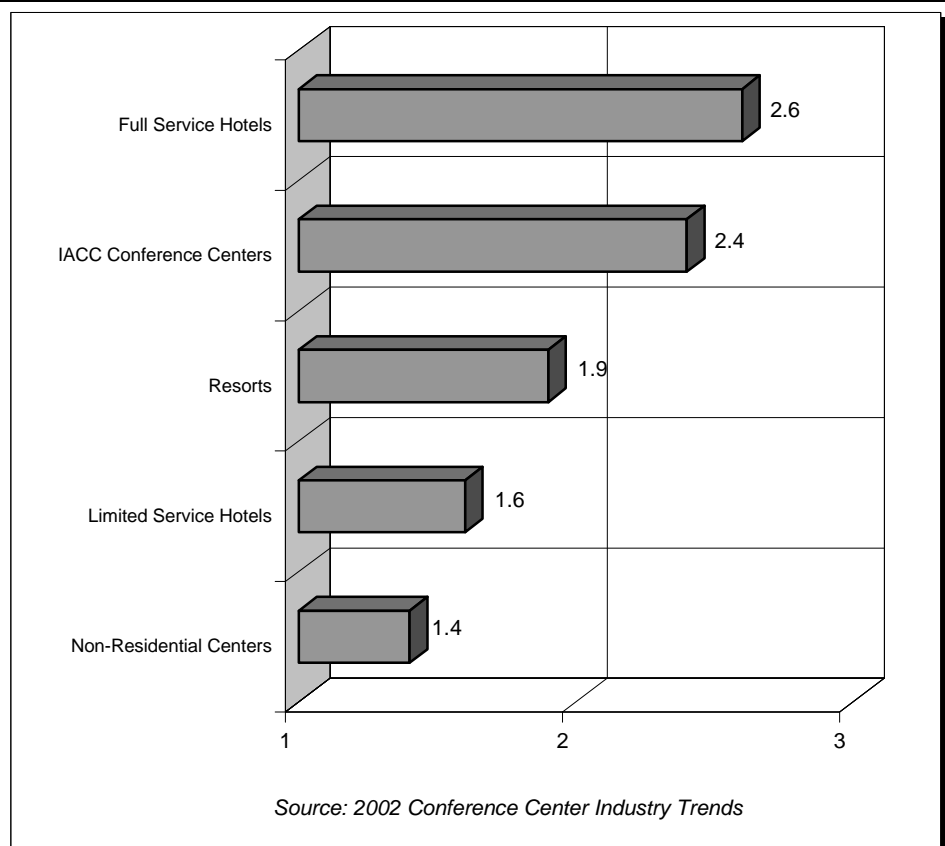
Figure 5-6
Source of Bookings for Conference Centers



Local demand sources generate about half of all demand for meetings at residential conference centers. Regional sources account for less than one-third of demand. National and international sources account for about one-fifth of overall meeting demand.

Figure 5-7 illustrates which property types conference center managers view as their biggest competition. A score of “1” indicates property types which are not competitors. A score of “2” indicates property types that are occasionally competitors. A score of “3” indicates property types which are highly competitive, according to conference center managers.

Figure 5-7
Sources of Competition



Conference center managers cite full service hotels as their biggest competition. Other IACC conference centers also pose substantial levels of

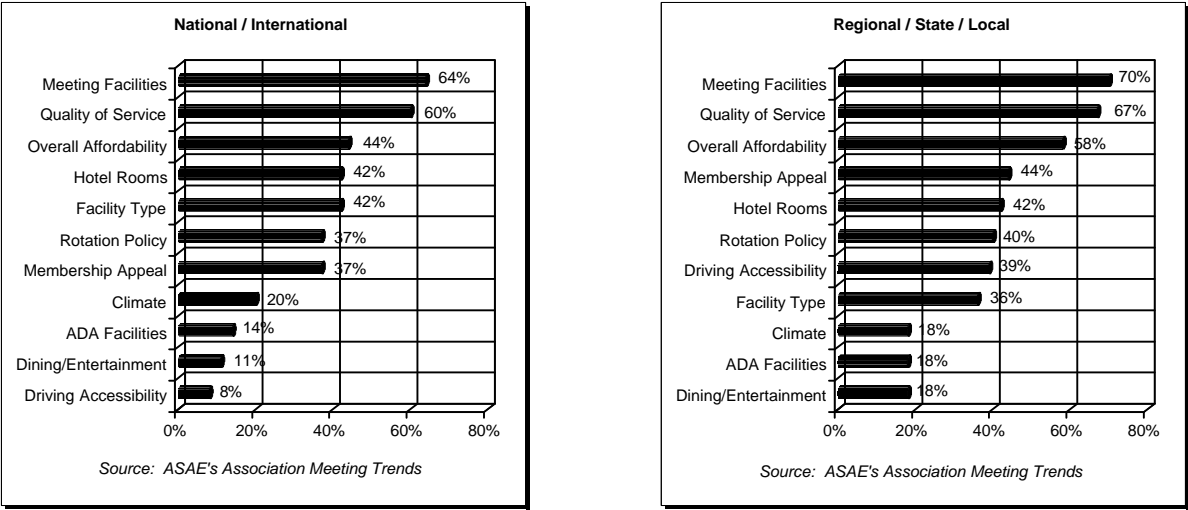
competition in many markets. Resorts are occasionally competitive. Limited service hotels and non-residential conference centers are only somewhat competitive, based on industry survey data from IACC.

Event Planner Location Criteria

In the meetings industry a relatively small number of people make decisions for a large number of people about where to hold meetings. Meeting planners compare relevant criteria about various potential meeting locations and make plans for their companies, clients, or organizations. Therefore, it is critical to understand what criteria meeting planners deem most important in the current meetings market environment.

Figure 5-8 shows the criteria that convention, association, and meeting event planners consider most important in selecting a destination for their events. Meeting planners cited the following criteria as “very important” in a survey conducted by the American Society of Association Executives (“ASAE”).

Figure 5-8
Share of Event Planners Citing Factors as “Very Important”, National vs. Regional



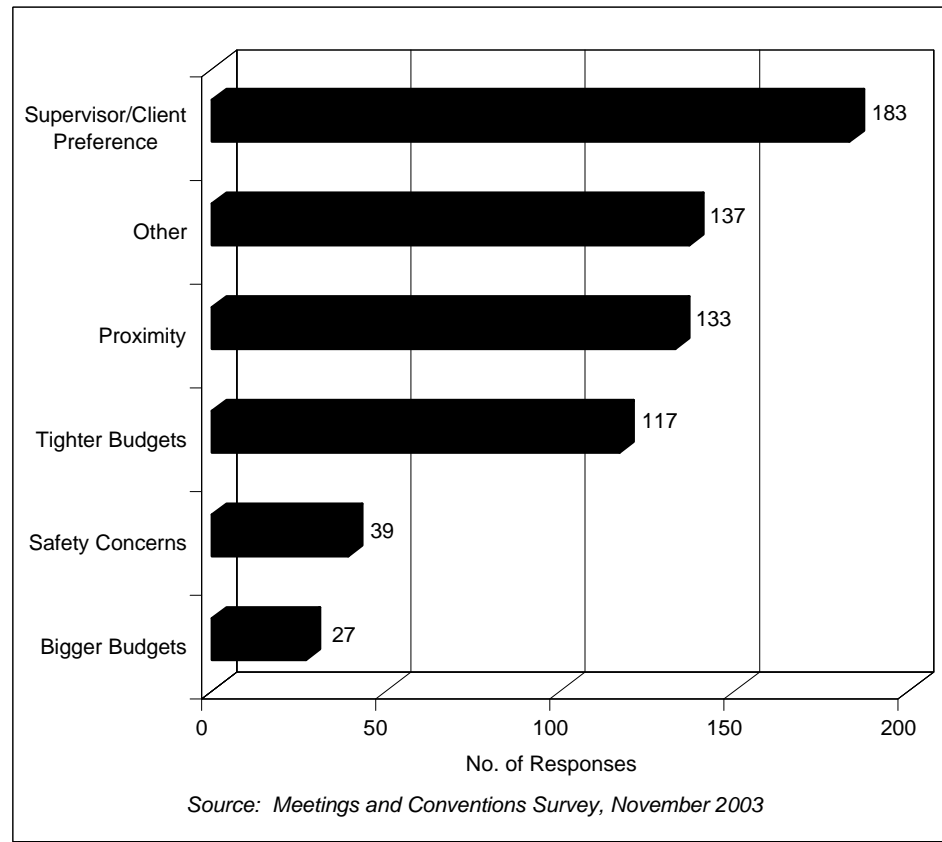
The survey asked respondents whether various site selection criteria were very important. The answers of national / international and regional / state / local event planners were very similar. The quality of meeting facilities, service, affordability, and hotel room supply are key criteria for both groups. Although affordability is very important to many meeting planners,

an even larger portion of meeting planners indicate a high quality of service is very important. Not surprisingly, the attractiveness and appropriateness of the actual meeting facility is very important to most meeting planners. One important factor not included in the survey is air access. In a later section of this report HVS interviewed meeting planners to determine how important this concern is for the subject market.

Meetings & Conventions also conducted a survey to identify meeting planners' priorities, especially among those considering new meeting locations. Of those meeting planners seeking new locations for their 2004 meetings, the most frequently given reason for the search for a new location was a desire for a new location on the part of a client or supervisor. Of the 574 meeting and event planners surveyed, 68 percent said they are seeking a new location for their event or meeting in 2004.

Figure 5-9 shows the most frequently reported reasons given for the desire to switch locations.

Figure 5-9
Reasons for Changing a Meeting Location



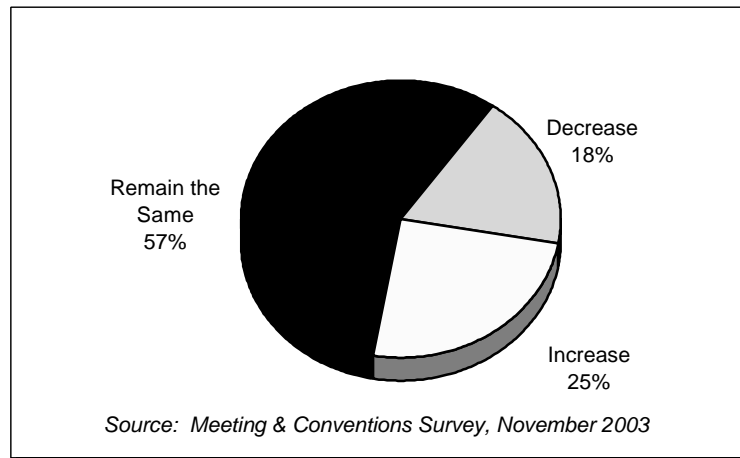
The most frequently reported reason for the desire to change meeting or event locations was supervisor and / or client preference. 'Other' was listed as the second-most common response, with proximity of the meeting to attendees and tighter budgets reported third and fourth, respectively.

Meeting Budgets

While the number meetings and conventions were curtailed by the recent downturn in the national economy, a survey of meeting and event planners conducted by Meetings and Conventions in November of 2003 indicates that the meetings and conventions industry may be on the rebound. Meetings and Conventions surveyed 574 meeting and event planners, and the results indicates that the majority of the planners are considering new meeting locations and are working with budgets that meet or exceed their 2003 levels.

Figure 5-10 shows the expectations of the meeting planners as to their 2004 meeting budgets.

Figure 5-10
Meeting Planner Expectations of 2004 Meeting Budgets



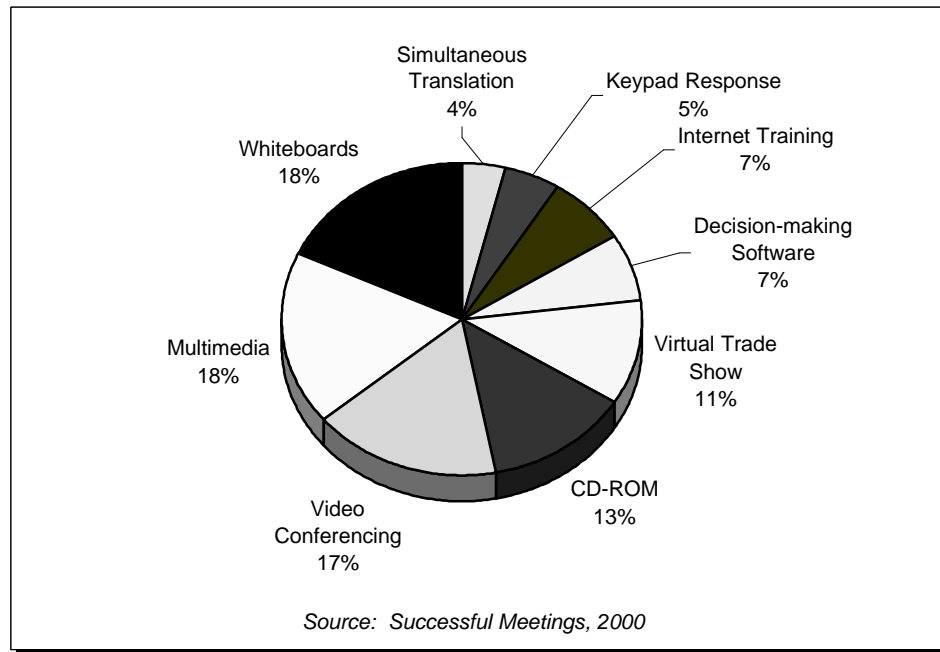
The majority of meeting and event planners, 57 percent, expect their 2004 budget will remain the same as last year, while 25 percent expect it will increase and 18 percent expect it will decrease from their 2003 levels.

Use of Technology in Meeting Facilities

Overall, the meetings and conferences industry uses a moderate amount of technology during events, typically computers with Internet access and audiovisual presentation equipment. The meeting and conference industry lags behind other leading industries in terms of incorporating new technologies. The majority of conventions and conferences still require only basic technological amenities like a laptop or video projectors, items that most facilities possess.

Multi-media, whiteboards and videoconferencing are the three most commonly used technologies, as shown in Figure 5-11.

Figure 5-11
Technology Used to Deliver Meeting Content



The variety of methods used for delivering meeting content indicates the need for conference center facilities to be as flexible as possible in their configurations and to have design elements that enable the use of a wide variety of technologies. The number of different methods suggests that portable elements or easily adaptable elements are preferred to permanent, built-in elements.

Emerging Industry Trends

Over the past few decades, the meeting and convention industry has evolved dramatically from a budding industry to a more mature one that has become an important driver of the national economy. Currently, industry expenditure estimates are over \$40 billion per year, according to Meetings & Conventions. As an established industry, the rapid growth of the last four decades is not likely to persist. However, continued evolution and growth can be expected on a controlled scale. HVS has identified the following emerging industry trends.

- **Supply and Demand Equilibrium** — Because so many conference facilities utilize public funding, the expected relationship between

supply and demand found in the private sector does not necessarily hold true for the meeting and convention industry. Public entities are motivated to develop conference centers because they seek adequate facilities for local user groups; hope to generate urban impacts in certain areas of the community; or aim to attract new visitor spending to the market area. These public entities are not constrained by the need to achieve a return on investment in the facility. Rather, conference centers are considered “loss leaders” which can increase the overall level of expenditures in the local economy. The consequence of this disengagement between the rationale for an increase in supply and the given available demand has the potential to lead to an overbuilt situation, as currently planned new construction and expansions are completed. However, public entities are constrained by limitations on tax resources to support these developments. If conference centers do not produce the expected economic impacts, the justification for increasing public support of conference center development will become less politically viable. These political constraints are likely, in the long run, to keep the supply of space commensurate with demand.

- **Quality of Supply** — As the industry has matured and competition among cities has become more intense, meeting planner expectations for quality have increased. For example, proximity of full service hotels to conference centers has become a primary determinant in the decision of whether to locate a meeting at a particular location. Cities lacking suitable hotel properties typically lose business to cities with a good “hotel package.” Similarly, advanced communications technologies in conference centers are now routinely expected. Furthermore, surveys of meeting planners show that their expectation for a higher quality of service has become one of the most important site selection criteria. In an oversupplied market, quality expectations are likely to increase in importance.
- **Emergence of “Destination Meeting Resorts”** – Several resort communities have emerged as primary meeting resort destinations, such as Las Vegas and Orlando, among others. These cities have undergone rapid growth in the supply of hotels and resort conference facilities that are quickly absorbed with new business.

They have in common a strong tourist appeal, attractive climate, and broad appeal among different segments of event attendees. Their ability to attract a large number of attendees is a prime consideration in site selection decisions by meeting planners. Cities with such strong destination appeal are likely to continue to be the most successful conference destinations in terms of overall attendance.

- **Propensity to Travel** — Declining cost of travel (in real terms) and the increase in the propensity to travel has been a primary driver of long-term growth in the meetings industry. Recent events and geopolitical concerns that temporarily reduced the ability and desire to travel clearly demonstrated the importance of travel propensity to the industry. However, in the long-run, expansions in the transportation system and continued innovations that reduce costs and increase the ease of travel are likely to support the growth of the meeting industry.
- **Improved Communications Technology** — Over the past decade, industry experts have engaged in a great deal of speculation that improvements in telecommunications technology will supplant the need for face-to-face meeting. To date, there is only limited evidence that video conferencing or the telecommunications have become viable substitutes for in-person communication. Many meeting types still require person-to-person interaction to exchange ideas and information, and to build relationships. To the extent that improvements in communications technology have contributed to overall economic growth, it is possible this trend will foster additional growth in the meetings industry.

Several of the trends in supply and demand as well as emerging industry trends have implications for anyone considering the development of a full service hotel conference center. HVS summarizes some implications for the subject project below.

Implications for Flagstaff

Continued growth in the meetings industry depends largely on continued growth of the national and local economies. The recent economic recovery nationally has corresponded with some improved performance in the hospitality industry, broadly defined. The improving economy, combined

with industry survey data, suggests corporate travel budgets may increase in 2004 after several years of constraint. This could lead to resumed growth in demand for meetings in coming years.

Another current trend in the meetings industry suggests a shift from national to regional, state, and district events. State associations are increasingly looking towards the development of district meetings and specialized educational programming to keep their members engaged and involved on a more local level. Flagstaff is not positioned in terms of its size or level of overall visitor infrastructure to attract significant levels of national event demand. However, this trend toward district meetings may create opportunities for Flagstaff to capture newly emerging meeting demand.

In the following analysis, HVS will analyze comparable facilities, Flagstaff's demand potential, event planners' perceptions of the subject market as a conference destination, supply and demand in the hospitality market, and other factors that influence its overall group event potential. The answers to these questions will help HVS determine the appropriate type of facility for Flagstaff and the volume and character of meeting events likely to occur at the proposed facility.

6. Comparable Facilities Analysis

Introduction

The purpose of this section is to analyze a number of comparable facilities of similar size and scope. In this section, HVS compares the facility programs, demographic market factors, and performance measures of selected hotel conference centers around the nation. Selected facilities are comparable to the subject in several important ways. In particular, each is located in the downtown area of a secondary or tertiary meeting market. Each had the support of public incentives or public financing. Each facility has meeting space that has been certified by the International Association of Conference Centers (“IACC”). Finally, HVS reviewed facility programs to find close matches with the proposed hotel conference center, which is planned to have 250 hotel rooms, about 7,750 square feet of ballroom space, 10 breakout meeting rooms with 470 square feet each, four conference rooms offering 5,900 square feet of meeting space, an amphitheater, and a boardroom. In total the facility would have approximately 22,000 square feet of function space.

In this analysis HVS compares the proposed hotel conference center in Flagstaff to the selected facilities and their respective markets. This section focuses on market and facility characteristics that are important to the performance of urban hotel conference centers. Our examination of the performance of comparable facilities provides a basis for the projection of demand and financial operations of the proposed hotel conference center in Flagstaff.

Size & Scope of Comparable Facilities

HVS reviewed facility programs, market characteristics, and performance data for five comparable facilities. HVS searched for urban facilities in small markets that serve statewide, corporate and association meeting demand. In this section HVS analyzes the Chattanooga Hotel & Conference Center in Tennessee (IACC certified), the Renaissance Portsmouth Hotel & Waterfront Conference Center in Virginia, the Provo Marriott Hotel & Conference Center

in Utah (IACC certified), and the Tempe Mission Palms Hotel & Conference Center in Arizona.

The selected facilities are not expected to compete directly with the proposed facility in Flagstaff. A competitive set of properties is defined elsewhere in this report. Instead, these comparable projects, located elsewhere in the country, provide some background and precedent for a project of this size and scope. In this section we review the ways in which these other projects are similar or different to the subject and what these other projects may be able to teach us about the likely performance of the proposed hotel conference center in Flagstaff.

Table 6-1 shows a summary of the building programs of each selected peer facility. This table compares the peer average with the proposed subject.

Table 6-1
Comparison of Comparable Hotel Conference Centers

	The Chattanooga	Renaissance Portsmouth	Provo Marriott Hotel & Conf. Center	Tempe Mission Palms	Peer Average	Subject
Location	Chattanooga, TN	Portsmouth, VA	Provo, UT	Tempe, AZ	-	Flagstaff, AZ
Brand	Independent	Renaissance	Marriott	Independent	-	Independent
Operator	Benchmark	Crestline	Marriott	Destination	-	Benchmark
Number of Guest Rooms	202	249	331	303	271	250
Number of Breakout Rooms	8	7	19	13	12	14
Size of Boardroom	740	832	968	720	815	750
Size of Amphitheater	2,392	1,755	2,618	None	2,255	2,450
Size of Grand Ballroom	7,752	11,858	8,088	9,384	9,271	7,750
Net Function Space	25,000	24,000	28,000	22,000	24,750	22,000
Function Space per Guest Room	124	96	85	73	91	86

Sources: Facility websites, IACC, HVS Interviews

The selected comparable facilities offer between 202 and 331 hotel guest rooms. The proposed hotel conference center in Flagstaff would fall in the middle of this range with 250 hotel guest rooms planned. The comparable facilities offer between 22,000 square feet and 28,000 square feet of rentable function space. The proposed hotel conference center in Flagstaff would be at the bottom of this range with just under 22,000 square feet of function space. The selected comparable facilities have between seven and 19 breakout meeting rooms. The subject facility has plans for 14 breakout meeting rooms. The comparable facilities have between 73 square feet and 124 square feet of function space per guest room. The subject would have approximately 87 square feet of function space per guest room, according to preliminary building plans.

Most of the comparable facilities offer an amphitheater and a boardroom. The subject also includes plans for an amphitheater and a boardroom. One of the four comparable facilities has a national brand flag and corporate management. Two of the comparable facilities have independent brands managed by private operators. The property in Portsmouth has a national brand and a private operator. According to current plans the subject facility would be an independent brand with a private operator. The City of Flagstaff would own the hotel conference center and would pay a management fee to Benchmark Hospitality to operate the facility.

Brief Overview of Comparable Facilities

The **Chattanooga Hotel Conference Center** opened in April 2001 after the City of Chattanooga issued revenue bonds to support the project. This urban resort offers 202 hotel guest rooms and 25,000 net square feet of IACC-certified meeting and banquet space. The City of Chattanooga owns the property. Benchmark Hospitality operates the facility. It is the only IACC-certified property serving the Chattanooga market area.

The hotel conference center is situated in the historic Southside area of downtown Chattanooga. Nearby amenities include the Warehouse Row shopping district. The Tennessee Aquarium, BellSouth Park, and the Tennessee River form a newly revitalized riverfront entertainment district approximately ten blocks away. Directly adjacent to The Chattanooga is the newly expanded Chattanooga Convention Center. The new facility offers a total of 312,000 square feet, which includes 100,000 square feet of clear span exhibit space, 21 business meeting rooms and six ballrooms.

As the only upscale hotel conference center of its size in the Chattanooga market, this property attracts a substantial amount of group demand. Approximately 45 percent of the total room night demand is group, according to HVS interviews with management. The group demand is approximately 75 percent corporate and 20 percent state association business. The remaining five percent of group business comes from social, military, educational, religious, or fraternal (“SMERF”) gatherings. Approximately 65 percent of all group business consists of packages that could include meeting space, meals, and entertainment. Based on performance statistics and interviews with sales managers, HVS estimates the conference center induced approximately 17,000 room nights for the Chattanooga Hotel Conference Center.

The **Tempe Mission Palms** opened in 1985 in downtown Tempe, Arizona. This urban resort offers 303 hotel guest rooms and 22,107 net square feet of IACC-certified meeting and banquet space. The O.P.E.R.S. pension fund in Ohio owns the property. Destination Hotels & Resorts operates the facility.

The hotel conference center is situated in the center of a commercial downtown district with a variety of shops and restaurants surrounding the property. Nearby amenities include the Tempe Town Lake, Beach Park, and the Sun Devil Stadium. The property is only four miles from the Phoenix Sky Harbor International Airport.

As a premier upscale hotel conference center in Tempe, this property attracts a substantial amount of group demand. Approximately 63 percent of the total room night demand is group, according to HVS interviews with management. The group demand is approximately 50 percent corporate and 30 percent state association business. The remaining 20 percent of group business comes from social, military, educational, religious, or fraternal (“SMERF”) gatherings. Approximately 45 percent of all group business consists of packages that include meeting space, meals, and entertainment. Based on performance statistics and interviews with sales managers, HVS estimates the conference center induced approximately 21,700 room nights for the Tempe Palms Hotel in 2003.

The **Provo Marriott Hotel & Conference Center** opened in 1998 in downtown Provo, Utah. This urban resort offers 330 hotel guest rooms and

28,000 net square feet of meeting and banquet space. Sunstone Hotels owns and operates this property.

The hotel conference center is situated in downtown Provo. Nearby amenities include the Provo Towne Centre, Utah Lake, Seven Peaks, and the Provo River. The property is approximately two miles from Brigham Young University. Major corporations in the market area include Intel, Micron, Novell, Nestlé, and Geneva Steel.

As the only upscale hotel conference center in Provo with IACC-certified meeting space, this property attracts a substantial amount of group demand. Approximately 35 percent of the total room night demand is group, according to HVS interviews with management. The group demand is approximately 40 percent corporate and five percent state association business. About 25 percent of group demand comes from the tour and travel segment. The remaining 30 percent of group business comes from social, military, educational, religious, or fraternal (“SMERF”) gatherings, including sports and university groups. Because of a relatively large portion of social, sports, and tour groups only about 25 percent of all group business consists of packages that include meeting space, meals, and entertainment. Based on performance statistics and interviews with sales managers, HVS estimates the conference center induced approximately 17,300 room nights for the Provo Marriott Hotel in 2003.

The **Renaissance Portsmouth Hotel & Waterfront Conference Center** opened in January 2001 after the City of Portsmouth issued bonds to support the project. This urban resort offers 249 hotel guest rooms and 24,335 net square feet of IACC-certified meeting and banquet space. Highland Hospitality bought the property from the original ownership parties, which included Crestline, Stormont, and the City of Portsmouth. Crestline Hotels operates the facility.

The hotel conference center is situated in downtown Portsmouth’s historic Olde Towne district. The Norfolk International Airport is approximately 10 miles northeast of the hotel conference center. The property overlooks the Elizabeth River and the Norfolk skyline. The Children's Museum of Virginia, the Virginia Sports Hall of Fame, and the Naval Shipyard Museum are within walking distance. The Elizabeth River ferry provides access to Norfolk

where activities include shopping at MacArthur Center and minor league baseball at Harbor Park.

As the only upscale hotel conference center of its size in Portsmouth, this property attracts a substantial amount of group demand. Approximately 47 percent of the total room night demand is group, according to HVS interviews with management. The group demand is approximately 50 percent government and 25 percent state association business. In 2003 about 20 percent of group demand was corporate. The remaining five percent of group business comes from social and educational events. Less than 10 percent of group business consists of packages that include meeting space, meals, and entertainment. But a no-rooms package that focuses on local catering has been very successful. Based on performance statistics and interviews with sales managers, HVS estimates the conference center induced approximately 21,800 room nights for the Portsmouth Renaissance Hotel. Most of this business has been drawn from groups that otherwise would meet in the Marriott or Sheraton in Norfolk, Virginia.

HVS will analyze this group of comparable facilities in greater detail throughout this section. By understanding key market and demand factors for this group of comparable developments we will gain an understanding of the potential for a hotel conference center in Flagstaff of similar size and scope.

Induced Room Night Demand

A primary justification for investment in meeting space is its potential to attract group events and business that would not otherwise use the hotel property. In many cases, local governments justify public investment in hotel conference centers because the additional meeting space attracts out-of-town groups that otherwise would not visit the community. One measure of the impact of meeting space on the hotel property and the community at large is induced room night demand. The room nights that would not be booked in a community, but for the added meeting and conference space, are considered “induced demand” generated by the conference center.

Table 6-2 shows a summary of the induced room night demand generated by comparable conference facilities around the nation.

Table 6-2
Induced Room Nights

	The Chattanooga	Renaissance Portsmouth	Provo Marriott Hotel & Conf. Center	Tempe Mission Palms
Meeting Space (Sq. Ft.)	25,000	24,335	28,000	22,107
Total Room Nights	68,600	64,500	72,300	80,500
Group Room Nights	30,900	30,300	25,300	50,700
Corporate	75%	20%	40%	50%
Association	20%	25%	5%	30%
Govt/SMERF/Tour	5%	55%	55%	20%
CMP as % of All Group Business	65%	10%	25%	45%
Induced Room Night Estimates	17,000	21,800	17,300	21,700
Induced Room Nights Per Sq. Ft.	0.68	0.90	0.62	0.98

Source: HVS International

The four comparable projects under review offer approximately the same amount of meeting space as the proposed hotel conference center in Flagstaff. HVS estimates induced room nights at these four comparable facilities were in the range of 17,000 room nights to 22,000 room nights per property during fiscal year 2003. This represents an ability to generate between one-half and one induced room night per net square feet of meeting space on an annual basis. Numerous factors can have a significant effect on a conference center's ability to generate induced room nights. But the range shown in the selected group of properties provides a guideline for induced room night estimates for the proposed hotel conference center in Flagstaff.

Population & Income Data

Although there is no direct correlation between the size of a market's resident population and demand for conference space, population data reveals trends in the overall economic climate of an area and its ability to support local group events. Demographic trends can also be an indicator of a community's ability to provide and maintain visitor-related infrastructure and attractions. High population or income density and/or growth rates can indicate significant capacity to support local meetings and banquets and a likelihood that the area will add to its existing urban attractions. Strong population growth also suggests an increasing commercial and fiscal base to support public facilities. Population changes often reflect underlying trends in business activity and the attractiveness of an area as a place to live, work, and visit.

Table 6-3 shows population, per capita income, aggregate personal income, and total employment figures for the comparables markets. The information is presented for each market's Metropolitan Statistical Area ("MSA").

Table 6-3
Population and Income of Comparables Markets

Market	MSA Population 1990	MSA Population 2000	MSA Population 2004	% Chg	Per Capita Income	Personal Income (\$million)	Total Employment
Flagstaff, AZ	102,200	122,200	128,600	1.7	21,410	2,754	75,707
Provo, UT	264,600	355,800	391,300	2.8	19,201	7,514	215,676
Chattanooga, TN	424,500	455,800	471,100	0.7	26,063	12,279	306,068
Portsmouth/Norfolk, VA	1,450,900	1,576,800	1,634,900	0.9	25,168	41,147	1,023,966
Tempe/Phoenix, AZ	2,245,800	3,087,400	3,383,900	3.0	28,237	95,549	2,109,481

**Income and employment data based on 2004 estimates.*

Sources: Woods & Poole, HVS International

According to Woods & Poole Economics, a nationally recognized demographic research company based in Washington D.C., the Flagstaff MSA is the third largest population center in the State of Arizona, behind Phoenix and Tucson. Two of the selected peer markets are located in large metropolitan areas and two are located in smaller urban markets. Among the comparable projects, the one in Tempe/Phoenix has the largest market. It has approximately 3.4 million residents. The Flagstaff MSA is the smallest of all these markets in the peer set, with about 129,000 residents. Provo and Chattanooga also have populations of less than a half million people. The Portsmouth/Norfolk MSA has roughly 1.6 million residents. All five MSA's experienced population growth throughout the 1990's. Provo, Utah and Tempe/Phoenix have exhibited the fastest population growth since 1990. Flagstaff exhibited the third fastest population growth rate among the group of selected peer markets.

Income and employment statistics can provide insight into the general health of the area's economy. The overall health of the area economy has implications for its ability to generate locally-based event demand, sustain and develop visitor infrastructure such as hotels and attractions, and make ongoing public investments that create a local image that is attractive to group, business, and leisure tourists. The size of each peer market's local economy varies significantly. Aggregate personal income in Tempe/Phoenix is projected to be approximately \$96 billion in 2004. For comparison

purposes, HVS shows personal income in 1992 dollars. The aggregate personal income in the Provo market was about \$7.5 billion. Total employment ranges from about 216,000 jobs in Provo to approximately 2.1 million jobs in Tempe/Phoenix.

Per capita personal income reflects the relative spending capacity of local residents, and provides another benchmark for assessing the region's ability to develop and maintain both public and private services and attractions that help make an area an attractive place to live and visit. The Flagstaff MSA has a modest per capita income level compared to most of the selected comparables. Per capita income is estimated to be approximately \$21,400 in 2004. In the peer markets, per capita income levels range from about \$19,200 in Provo to about \$28,200 in Tempe/Phoenix.

Based on market size and demographics, Flagstaff's closest peers in the selected set are Provo and Chattanooga. Induced room night estimates are likely to be most consistent with these properties. Flagstaff is the smallest of the markets under review. HVS will consider this and other market factors in our demand analysis. However, all four selected facilities are similar to the proposed Flagstaff property with respect to their building programs.

Implications of Peer Analysis

Each of the four selected peer facilities is positioned as one of the most upscale properties in their respective markets. Their high-end meeting and banquet spaces allow them to attract more group business than they otherwise would capture. Conference space at each facility is responsible for a significant amount of induced room night demand. The proposed hotel conference center in Flagstaff is very comparable to the selected peer facilities in terms of size, scope, and an emphasis on targeting group business. The market population in Flagstaff is smaller than each of the peers. But all are considered tertiary meeting markets that focus on in-state group business. Furthermore, all four properties exhibit a fairly narrow range of induced room nights that is consistent with industry norms.

7. Analysis of Group Demand

This section evaluates potential demand for meeting and conference events in Flagstaff. Based on this analysis, HVS estimates the induced room night demand the new conference facility is likely to generate. HVS conducted the following tasks to assess the demand potential for a full-service, upscale hotel conference center in downtown Flagstaff, Arizona:

- Analyzed lost business reports,
- Reviewed focus group data,
- Interviewed corporate and institutional meeting planners, including Northern Arizona University, and
- Surveyed state association event planners concerning their perceptions of Flagstaff and their facility needs.

The preceding tasks, combined with knowledge of industry trends and the analysis of comparable facilities in previous sections, provide HVS with a basis for projecting events, attendance, and induced room night demand for the proposed hotel conference center in Flagstaff.

Lost Business Analysis

The Flagstaff CVB maintains a list of potential events that previously considered Flagstaff, but were lost to other markets or did not occur in Flagstaff for some other reason. This list includes events that could have used existing hotels or meeting facilities in Flagstaff. But it also includes events that could not be held in Flagstaff because there is currently not an adequate meeting or conference facility. The CVB tracks information on each event including: facility requirements; peak room nights; and the year the event is planned.

Since May 2002, when the CVB began maintaining lost business data, there have been 23 events lost, which were to have occurred between 2002 and 2005.

Table 7-1 lists each of the lost events recorded by the Flagstaff CVB. Lost business is shown in chronological order of event dates.

Table 7-1
Lost Business Summary

Organization	Peak Room Nights	Banquet Capacity	Theater Capacity	Meeting Rooms	Meeting Room Capacity	Year
Arizona Department of Water Resources	100	-	-	4	25	2002
DNA Peoples Legal Services, Inc.	30	100	-	-	-	2002
Navajo Nation	70	-	-	1	70	2002
Pasco	10	-	-	1	10	2002
Private Party	-	-	-	1	40	2002
The Journey	90	-	90	-	-	2002
U.S. Department of Education	2	-	-	1	50	2002
U.S. Geological Survey	30	-	-	1	30	2002
Arbonn International	-	-	30	1	30	2003
Arizona State Association of Letter Carriers	200	200	-	N/A	N/A	2003
Jehovah's Witness	-	1,000	-	1	50	2003
Tau Beta Pi Association	35	55	-	3	60	2003
U.S.D.A. Forest Service	15	-	-	1	30	2003
U.S.D.A. Law Enforcement	70	-	-	1	70	2003
WholeExpo	40	10,000 SF	-	2	50	2003
A.C.A.A.	45	90	-	1	100	2004
Arizona Community Action Association	45	150	-	3	50	2004
Cole Family Reunion	-	150	-	1	150	2004
Labor Market Information Training Institute	225	225	60	2	30	2004
Rocky Mountain Electrical Lead	18	40	-	1	24	2004
Western Outdoor Writers Association	250	250	-	N/A	N/A	2004
AZ Center for Medieval & Renaissance Studies	120	120	-	2	60	2005
KKC Family Reunion	30	150	-	1	150	2005

Source: Flagstaff Convention & Visitors' Bureau

The majority of these events require both hotel rooms and meeting space. The average requested room block among groups requesting lodging was 75 rooms. Based on CVB data, HVS estimates that these events represent more than 1,400 lost room nights for the Flagstaff lodging market.

Meeting planners indicated the need for banquet space with seating capacity up to 1,000 people. Most groups that reported a need for banquet space required seating capacity for 150 to 250 people. Three groups indicated a desire for a fixed-seat amphitheater with between 30 and 90 seats. Most groups reported the need for between one and four breakout meeting rooms. They require meeting rooms with capacities of between 10 and 150 people. Lost business data indicates the importance of having flexible, divisible function spaces that can accommodate a wide range of group sizes simultaneously.

Focus Group Data

The Flagstaff CVB conducted focus groups with 37 meeting and event planners in October 2003. Participants represent potential corporate, government, tour, association, and SMERF clients for the proposed hotel conference center in Flagstaff.

Table 7-2 lists focus group participants. Several focus group participants indicated they specialize in a specific meeting segment. The table shows these segments.

Table 7-2

Focus Group Participants

Meeting Planner Organization	Meeting Segment	Meeting Planner Organization	Meeting Segment
A Daley Event	Travel/Tour	Meeting Wise	N/A
American Society of Radiologic Technology	Association	National Council for Prescription Drugs	Association
Arizona Academy of Family Physicians	Association	OutSource Management	Corporate
Arizona Dental Association	Association	PASCO	N/A
Arizona Osteopathic Medical Association	Association	Phillips Petroleum Company	Corporate
Association Management Solutions	Association	Premier, Inc.	Corporate
Bankfirst, Inc.	Corporate	Quality Business Services	Corporate
Baskow & Associates	N/A	Reaction Management	N/A
Carlson Wagonlit	Corporate	Rio Salado College	SMERF
Center for Professional Development	N/A	Rosenbluth International	Corporate
Chase Manhattan Mortgage Corp.	Corporate	Scarritt Groups, Inc.	N/A
Consultants in Meeting Management	N/A	Strategic Meetings	N/A
Convention & Group Services	N/A	The Conference Connection	N/A
Cox Communications	Corporate	The Hallstrom Group	Corporate
Honeywell	Corporate	The Marketing Department	N/A
Labor Market Information Training Institute	Government	University of New Mexico School of Medicine	SMERF
Management Plus	SMERF	World Travel BTI	N/A
Meeting Planning Plus	N/A		

*N/A indicates meeting segment focus was not available or the planner serves various segments.

Source: Flagstaff CVB Focus Groups

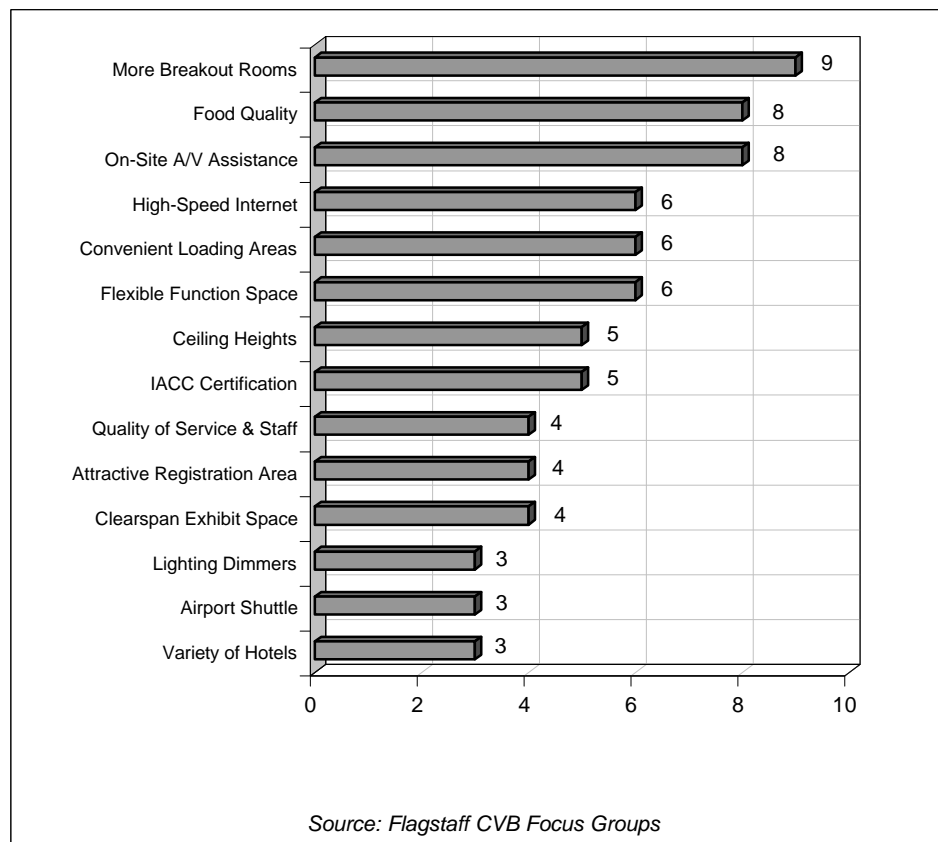
The focus group included 11 corporate meeting planners and six association meeting planners. Three meeting planners focus on SMERF events. The focus group also included one government meeting planner and one meeting

travel/tour group meeting planner. Other meeting planners serve various meeting segments or did not specify a particular meeting segment focus.

Focus group discussions reveal a number of important priorities for event planners as they make decisions about where to locate their meetings, conferences, tradeshow, and training seminars. HVS tallied the number of times meeting planners identified certain criteria as key factors for making decisions about where to hold an event.

Figure 7-1 summarizes the most frequently cited priorities that focus group participants identified for the proposed hotel conference center.

Figure 7-1
Number of Times Meeting Planners Cited Key Criteria



Meeting planners clearly believe Flagstaff's group business is limited because of meeting space and the lack of a larger conference facility. Focus group participants indicated the need for more meeting space and more breakout rooms than existing facilities offer in the Flagstaff market. The quality of food service and having on-site audio visual technicians are also two clear priorities among focus group participants.

As more hotels and conference centers upgrade their technology the competitive environment necessitates planning for high-speed internet access and modern audio and video equipment. Multiple loading docks and convenient loading and unloading areas are similarly important. Because a facility in the Flagstaff market will have to target a number of group segments in order to be successful, it is also imperative to have flexible function spaces that allow different configurations for user groups with various space needs.

Meeting planners also want adequate ceiling heights. Ceilings in large meeting rooms or ballrooms should be at least 18 feet to comply with industry standards. Smaller breakout rooms can have proportionately lower ceiling heights. Five meeting planners mentioned a preference for having meeting space consistent with standards set by the International Association of Conference Centers ("IACC"). However, they did not think it was necessary. IACC certification is not an essential factor for group business in Flagstaff.

Four focus group participants also indicated the importance of a courteous staff and a high level of service as an important factor to attract group business. It is likely that a larger number of focus group participants believe this is an important priority, but believe it is an obvious point that they did not need to mention. A similar number of participants indicated a desire for an attractive registration area. Clear span exhibit space is also important for the participants who plan tradeshow and events with exhibits.

Three focus group participants noted the importance of having lighting systems with dimmers in the meeting and banquet rooms. The same number of planners indicated their preference for having a variety of nearby hotel properties. Different brands and different price points at hotels can sometimes help to boost event attendance for meeting planners. Finally,

three focus group participants specifically noted the importance of having shuttle service from the airport. Numerous other meeting planners have cited the difficulty of accessing Flagstaff by air as a significant obstacle to attracting regional and national group business.

Meeting Planner Interviews

An essential component of this analysis includes detailed interviews with a relatively small number of corporate, educational, and institutional meeting planners who may have an interest in holding events at the proposed conference center. The data collected during these interviews is very important because it allows meeting planners to share candid views about the subject market and the proposed project under conditions of confidentiality. HVS does not attribute specific findings to individual meeting planners or their organizations. Moreover, the interview technique provides more flexibility than traditional surveys which seek answers that can be measure, classified, and categorized. This allows HVS to have a more thorough understanding of how meeting planners view the proposed project and the likelihood that they would hold events at the subject facility.

HVS conducted interviews with 22 corporate and institutional meeting planners. We also interviewed four professional meeting planners who represent numerous corporate meetings. In these interviews HVS focused on identifying potential demand from the corporate meeting segment as well as meeting facility needs from local institutions such as Northern Arizona University and the U.S. Forest Service. HVS asked meeting planners about their facility needs and their perceptions of Flagstaff as a meeting destination. Because of their knowledge of the meetings market and their relationships with major employers in the state, these meeting planners are in a unique position to provide insights about the potential to have corporate and educational events in Flagstaff. (Later in this section HVS presents findings from a separate survey of association meeting planners.)

Table 7-3 shows a list of organizations who participated in the HVS interviews. Several other corporate meeting planners were solicited for interviews, but were unable or unwilling to participate at this time.

Table 7-3
List of Interview Participants

Corporations	College & University
APS	Alumni Relations
Caremark (Advance PCS)	Arizona Hospitality Research & Resource Center
Flagstaff Medical Center	Center for Sustainable Environments
Integrity Systems	Coconino Community College
Phelps Dodge Corporation	College of Business
Schaller Anderson	DuBois Conference Center
SWCA, Inc.	High Altitude Center
The Dial Corporation	Melinda McKay - Jones Lang LaSalle
Universal Technical Institute	School of Forestry
W.L. Gore Associates	Professional Meeting Planners
Government	Christina Tzavellas, MPI
N.A.C.O.G.	Diversified Management Services
U.S. Forest Service	Jamie Cook, CMP
U.S. Geological Survey	Professional Directions, Inc.

Source: HVS International

The above table categorizes the HVS interviews into four basic categories. The first category includes company employees at 10 large corporations who internally plan and organize various meetings and events for their specific corporations. The second category includes government employees at three major organizations that represent demand potential in the subject region. The next category includes meeting and event coordinators at Northern Arizona University and Coconino Community College. The last category includes four professional meeting planners who primarily plan corporate meetings and events in Arizona. Together these meeting planners represent hundreds of corporate meetings that take place in central and northern Arizona on an annual basis.

The interviews revealed several key findings with respect to demand potential and marketing strategies. These comments are summarized below.

- Flagstaff is a drive-in market. Therefore, marketing efforts should focus on in-state groups.
- Demand is likely to be seasonal because one of Flagstaff's greatest advantages is mild summer weather.
- Majority of corporate meeting planners believe Flagstaff is too far away for most of their meetings.

- Air service is currently a challenge for corporate meeting planners.
- Substantial demand from university groups seeking multi-purpose ballroom with capacity for up to 300 people.

Meeting planners indicated there is a high level of demand for corporate retreats. But these groups primarily seek resort destinations or outdoor-oriented settings. They also tend to be concentrated in Central Arizona and seek meeting space in upscale hotels in and around Phoenix. Many of these groups are not willing to travel to Flagstaff. Meeting planners indicate the lack of air service to Flagstaff is a major deterrent.

Meeting planner interviews also revealed perceptions about the current and proposed supply of hotel and meeting properties in Flagstaff. Interviewer comments are summarized below.

- Existing supply of hotels is heavily weighted toward value-oriented customers and price sensitive groups.
- Existing meeting facilities are too small and/or need upgrades. Some properties are outdated.
- Any new facility should have substantially more meeting space than existing properties in Flagstaff.
- Any new facility should be more upscale than existing hotel and meeting properties in Flagstaff.

In addition to Flagstaff's potential to attract corporate groups from out of town, local employers are likely to generate demand for events in several categories. Interviews with meeting planners at major health care, education, and government institutions revealed a need for additional meeting, conference, and banquet space in Flagstaff. Local area employers such as the Flagstaff Medical Center, the U.S. Forest Service, Northern Arizona University, and the Northern Arizona Council of Governments ("N.A.C.O.G.") indicate a need for break-out meeting rooms for groups of about 40 people; banquet or general session space for about 300 people; and conference space for up to 200 people.

Northern Arizona University (“NAU”) represents a substantial source of potential demand, especially for banquets and academic conferences. University meeting planners expressed the need for multi-purpose ballroom space in the market, especially for events with 200 to 300 people. Events include faculty banquets, scholarship award ceremonies, reunions, fundraisers, and special event banquets. Event planners also indicated the need for meeting rooms, especially for classroom-style presentations. Events include academic conferences, board meetings, workshops, and training symposiums.

At the same time, the existing DuBois Center does not represent as much competition as a facility of its size might. NAU’s DuBois Center hosts many events planned at the University. However, the facility does not represent a serious threat to the proposed facility for several reasons. First, the DuBois Center only allows events that have an educational mission. Social events are not generally booked at the facility. Moreover, the facility does not have an adjacent full-service hotel. Most groups utilize nearby dormitories for multi-day events, which makes it unattractive for many adult groups. Finally, some meeting planners indicated they felt the facility was too outdated to consider for their events. While NAU may represent a substantial source of demand potential for the proposed hotel conference center downtown, its current supply of meeting space does not represent a major source of direct competition for the subject.

Interviews provide a general overview of how several corporate and institutional meeting planners view Flagstaff. They also provide specific insights about the strengths and weaknesses of a particular market and particular facilities. When considered in the context of interviews we conduct in other markets, they can help us gauge the demand potential for group events. HVS also conducts surveys to supplement the findings from our interviews.

Event Planner Surveys

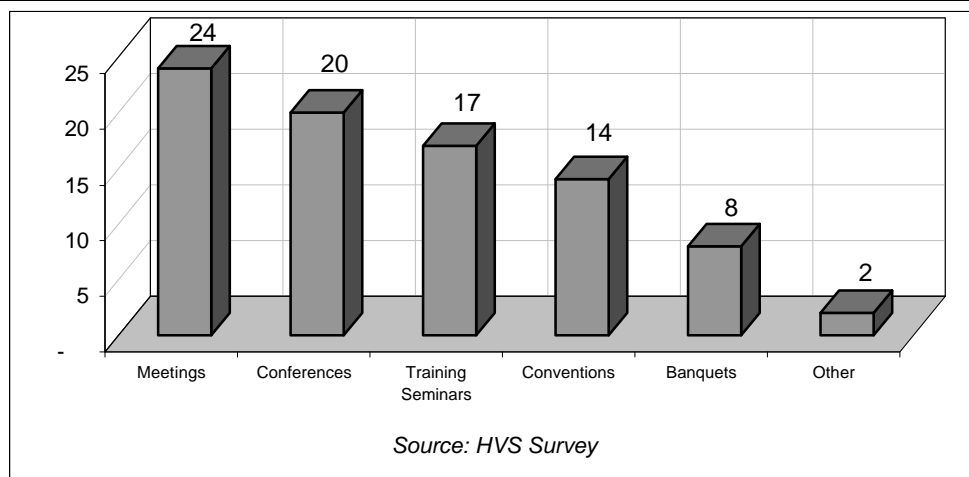
HVS conducted an on-line survey of state association meeting planners. This group represents potentially the largest source of demand for large meetings, conferences, and conventions. Because many of these groups are not located in Flagstaff, these events also have the greatest ability to generate economic impacts and additional room night demand for Flagstaff. In the convention industry a small number of event planners make event location decisions for

a relatively large number of delegates and attendees about where to hold events. HVS uses survey data to elicit expert opinion from a subset of these event planners to augment our understanding of demand potential in the subject market.

The HVS survey targeted event planners that are located in Arizona and have a membership listing in the directory of the Arizona Society of Association Executives. The survey produced 31 completed responses from state association event planners. HVS does not intend this survey to serve as a statistically valid measure for future demand at the proposed facility, but rather as a tool to measure the general interest level in the proposed hotel conference center and to determine how meeting planners view Flagstaff as a potential location for their events.

Figure 7-2 shows the most common types of events that the survey respondents plan or manage.

Figure 7-2
Most Common Event Types Planned or Managed by State Association Survey Respondents



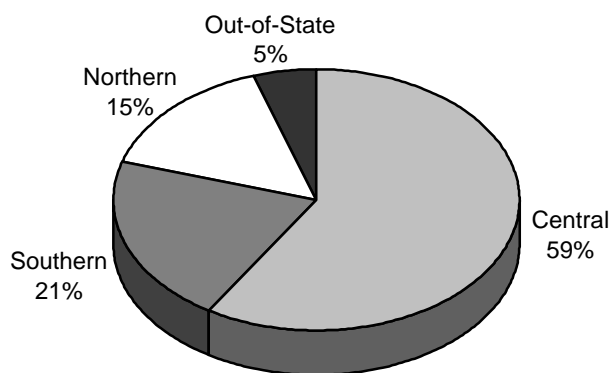
The respondents indicated that they were involved in a variety of events, with meetings cited most frequently. They also plan a significant number of conferences, training seminars, conventions, and banquets. For the purposes of this study we define small meetings to be gatherings of fewer than 100 people. Conferences are defined as meetings with 100 or more people.

Meetings, conferences, and training seminars primarily utilize meeting rooms. Conventions and banquets require larger banquet halls for general sessions and meals. Most conventions also require space suitable for exhibits. However, many of the meeting planners we surveyed indicated that lobbies and pre-function space is suitable for their exhibits. Other events include tradeshow, assemblies, and civic gatherings.

HVS asked event planners to describe the geographic origin of delegates to the largest events they plan. For the purposes of this survey HVS defined four potential geographic areas of origin for association members: Northern Arizona (includes Flagstaff); Central Arizona (includes Phoenix); Southern Arizona (includes Tucson); and Out-of-State.

Figure 7-3 shows where event attendees live, according to survey results from state association event planners.

Figure 7-3
Geographic Origin of Delegates



Source: HVS Survey

Not surprisingly, the largest portion (59 percent) of state association members resides in Central Arizona. Roughly 21 percent live in Southern Arizona. About 15 percent live in Northern Arizona. Only five percent live in another state. These findings correspond roughly to the distribution of Arizona's general population throughout the state.

Table 7-4 shows the meeting room and ballroom facility requirements for events planned by survey respondents.

Table 7-4
Facility Requirements for Events Planned by Survey Respondents

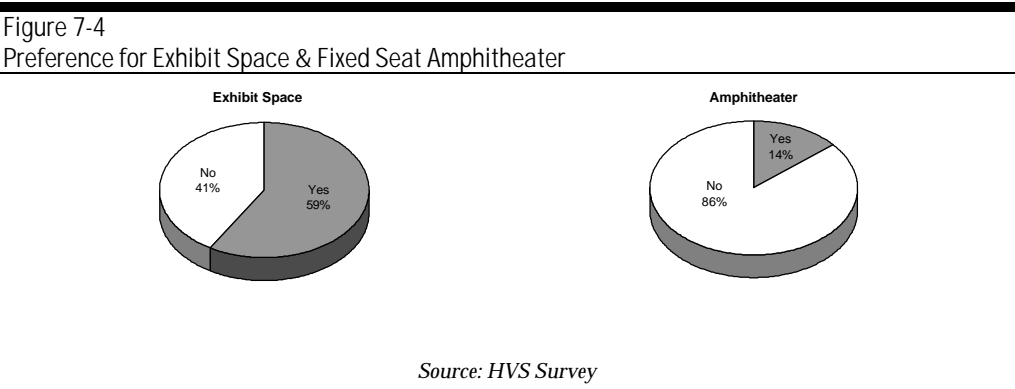
Function Space	Low	High	Average
Ballroom Capacity	100	600	250
Meeting Room Capacity	10	100	74
Number of Meeting Rooms	1	12	5

Source: HVS Survey

On average meeting planners need a ballroom with seating capacity for 250 people. But some events require banquet capacity for 600 people or more. Most meeting planners need multiple breakout meeting rooms that seat between 10 and 100 people. On average, meeting planners require five meeting rooms with seating capacity for 74 people. Preliminary facility plans include a grand ballroom, a fixed-seat amphitheater, and 15 additional meeting rooms that will allow the proposed facility to host almost all of the events identified by state association meeting planners as appropriate for Flagstaff. However, meeting planners indicated a strong preference for visiting Flagstaff during the summer. Therefore, it may be important that any conference center design allows for holding multiple events simultaneously.

The HVS Survey asked meeting planers to discuss their need for exhibit space and an amphitheater with fixed seats. Current plans include a fixed-seat amphitheater. Plans do not include dedicated exhibit space, although ballroom space and pre-function space may be suitable for light exhibits.

Figure 7-4 shows how meeting planners responded to questions concerning their need or preference for exhibit space and a fixed-seat amphitheater at the proposed conference facility.



The majority of event planners indicate they need exhibit space for their events. In most cases pre-function areas or banquet space is adequate for association exhibits. Most association event planners do not need a fixed-seat amphitheater according to our survey.

Table 7-5 shows the gross square feet of exhibit space needed for events planned by survey respondents.

Table 7-5
Exhibit Space Requirements Identified by Survey Respondents (in Square Feet)

Exhibit Space Needs
720
1,000
1,000
1,440
2,000
2,160
3,000
3,600
4,000
6,000
15,000
16,000
300,000

Source: HVS Survey

The majority of state association event planners who responded to the survey indicated they would use exhibit space if it were available. Exhibit space needs range from no exhibit space up to 300,000 square feet. However, most event planners use 6,000 square feet or less for exhibits. Moreover, the

majority of these events could use pre-function space or a multi-purpose ballroom for their exhibits. HVS interviews and focus group data also indicated meeting planners' willingness to use lobby space or other common areas for their exhibits.

None of the event planners indicated that a fixed-seat amphitheater was required for their events. However, a small number said they might use the amphitheater if it were available.

HVS assembled a list of facilities that respondents have utilized for their events in the past and the number of times each facility was listed. Each respondent had the option of listing several facilities that their group has used for past events.

Table 7-6 shows each facility that was listed more than once.

Table 7-6
Facilities Where Survey Respondents Have Held Events

Facility Name	Location	Number of Responses
Little America	Flagstaff	6
Prescott Resort & Conference Center	Prescott	5
Carefree Resort & Conference Center	Carefree	4
Pointe South Mountain Resort	Phoenix	3
Black Canyon Conference Center	Phoenix	3
Westin La Paloma Resort	Tucson	3
Orange Tree Golf Resort	Scottsdale	2
El Conquistador Hilton	Tucson	2
Forest Highlands Golf Club	Flagstaff	2
Scottsdale Resort & Conference Center	Scottsdale	2
Sedona Hilton Resort	Sedona	2
Tucson National	Tucson	2
Wyndham Garden	Phoenix	2

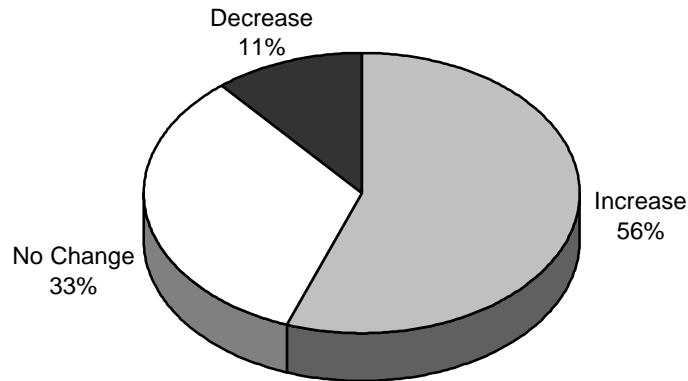
Source: HVS Survey

Respondents listed Little America, Prescott Resort & Conference Center, and the Carefree Resort & Conference Center most frequently. Hotel and conference center properties in Phoenix, Tucson, Scottsdale, and Sedona were also frequently chosen as event locations for a number of state association event planners.

Attendance trends and expectations are an important factor in projecting demand potential for any new facility. The HVS survey addressed whether event planners expect attendance at their events to increase, decrease, or remain the same over the next five years.

Figure 7-5 shows the result of the question regarding trends in attendance.

Figure 7-5
Expected Trends in State Association Event Attendance



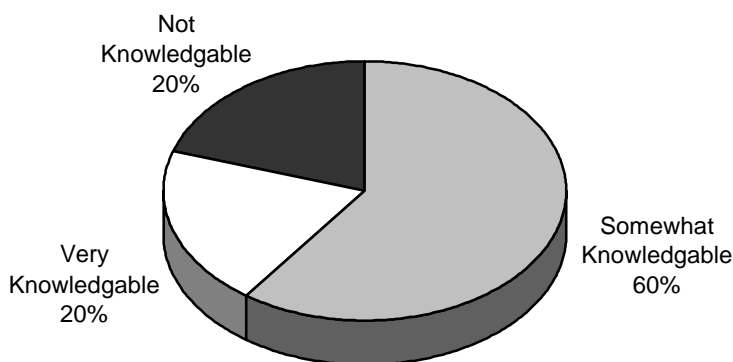
Source: HVS Survey

The majority of the responding association event planners anticipate that attendance at their events will increase during the next five years. Approximately 56 percent of respondents expect to see attendance increase. About 33 percent of respondents expect attendance to remain stable. Only 11 percent of event planners did not answer or anticipate a downward trend in attendance during the next five years.

Another factor that enters into meeting planners' decisions is their knowledge of a community and the event space in that community. Some event planners will be hesitant to book a major event in a community with which they are unfamiliar or in a building they have not visited. Therefore, HVS asked event planners to rate their level of knowledge of Flagstaff as a conference and meeting destination.

Figure 7-6 shows the level of knowledge among the responding event planners.

Figure 7-6
State Association Event Planner Knowledge of Flagstaff as a Meeting Destination



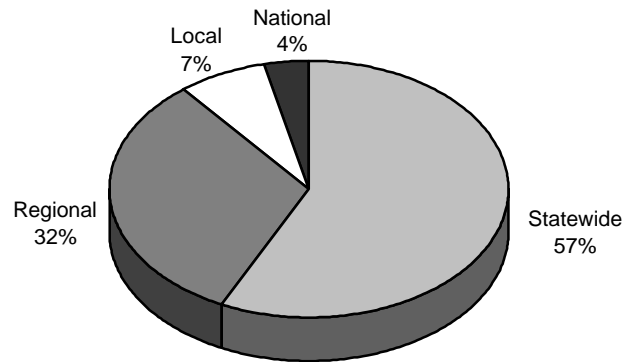
Source: HVS Survey

Among the respondents, only 20 percent consider themselves to be very knowledgeable regarding Flagstaff's characteristics as a conference/meeting destination. Approximately 60 percent classify themselves as somewhat knowledgeable. About 20 percent of state association event planners do not consider themselves knowledgeable about Flagstaff. These findings are not surprising due to the limited supply of meeting and conference facilities available in the Flagstaff market. But it represents significant potential to educate event planners if a new facility is developed.

In our survey, HVS asked event planners to indicate whether they viewed Flagstaff as a national, regional (multi-state), statewide, or local event destination. The perception among event planners of the role that Flagstaff can play in the market for events has implications for its demand potential as well as future sales and marketing strategies.

Figure 7-7 shows the views of event planners concerning Flagstaff's place in the overall market for events.

Figure 7-7
The Appropriate Scope for Flagstaff



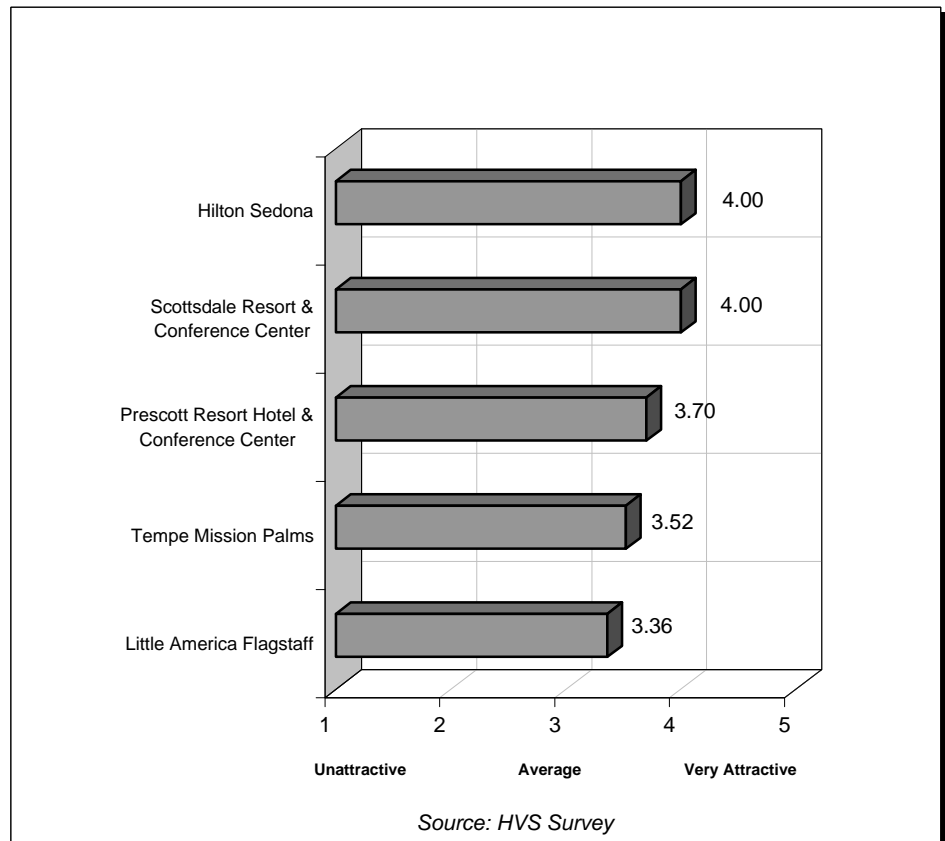
Source: HVS Survey

Responding event planners characterized Flagstaff most frequently as a statewide event destination. A significant portion of survey respondents think Flagstaff has the potential to attract multi-state regional events as well. Very few event planners view Flagstaff as a national event destination. Event planners also believe the proposed facility will serve a large number of local events; but they believe its potential scope is greater than just local events. This finding is consistent with HVS interviews and market research suggesting that Flagstaff should focus on the statewide, drive-in market for group events at the proposed conference facility.

HVS collected information about other facilities around the state and asked meeting planners about these venues. Respondents rated the overall attractiveness of a set of successful facilities located throughout Arizona.

Figure 7-8 shows the average rating for each facility.

Figure 7-8
Event Planner Ratings of the Overall Attractiveness of Intrastate Event Facilities

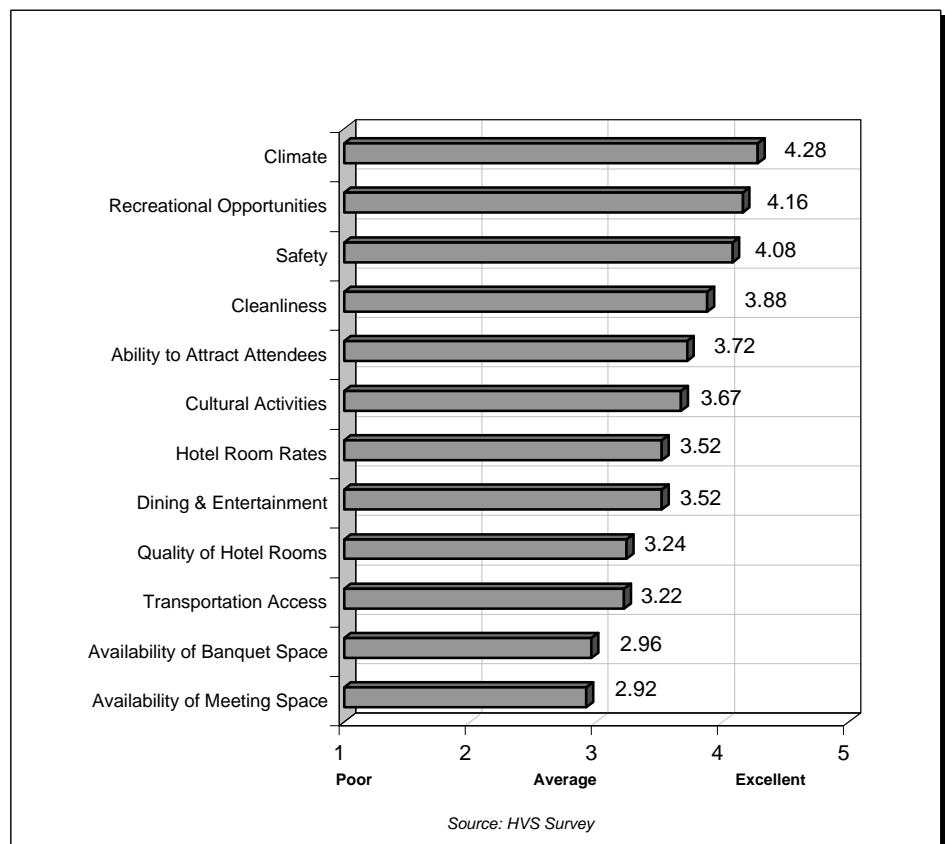


Event planners rated the Hilton in Sedona and the Scottsdale Resort & Conference Center among the most attractive facilities in the state for their events. The Prescott Resort Hotel & Conference Center and Tempe Mission Palms also received high ratings. Although above average, Little America received the lowest score among these five selected peer facilities. These scores may reflect a high level of expectations among state association meeting planners in Arizona, since many of these facilities offer a high level of service and amenities.

The HVS survey asked event planners to rate various attributes of Flagstaff in comparison to other cities in which they have held, or may hold events.

Figure 7-9 shows the survey results regarding Flagstaff's attractiveness, relative to other locations where meeting planners hold events, on a set of key site selection criteria.

Figure 7-9
Ratings of Flagstaff's Destination Characteristics



State association event planners rated Flagstaff between “good” and “excellent” on three destination characteristics, including climate, recreational opportunities, and perceived safety. Event planners specifically view Flagstaff as an attractive summer destination because its climate is cooler than the rest of the state. Event planners also view Flagstaff as clean. Event planners judge nearby cultural attractions, such as the Grand Canyon and Route 66, as positive influences on their decisions to consider holding an event in Flagstaff.

The most apparent obstacle to attracting more events to Flagstaff is its limited supply of banquet and meeting space. Event planners believe existing facilities are not big enough for their events. Moreover, event planners do not view the quality of Flagstaff’s hotel supply to be good for their events, although rates are attractive. Another major obstacle is transportation. Flagstaff’s air transportation service is very limited. As a result most event planners believe Flagstaff should focus on the drive-in market.

The surveys also invited respondents to discuss the strengths and weaknesses of Flagstaff as an event destination. These strengths and weaknesses provide a summary of factors that are important for Flagstaff’s potential to attract group business.

Table 7-7 shows a list of the specific comments of survey respondents regarding the perceived strengths and weaknesses of Flagstaff as an event destination, ranked in order of the frequency with which they were mentioned.

Table 7-7
Flagstaff’s Strengths and Weaknesses In Order of Frequency

Strengths	Weaknesses
Cool Summer Climate	Difficult Location / Transportation
Natural Beauty	Not Enough Meeting Space
Outdoor Recreation	Inadequate Hotel Supply
Location in Northern Arizona	Traffic Congestion / Crowds
	Cold Winters

Source: HVS Survey

Respondents overwhelmingly mentioned Flagstaff’s climate as a key strength for attracting group business. Most event planners specifically think of Flagstaff as a good summer destination because the weather is cooler than elsewhere in Arizona. Meeting planners also identified natural beauty and outdoor recreation as key strengths for Flagstaff. A small number of planners believe the location is convenient because they have members who live in Northern Arizona.

Meeting planners in our survey reinforced the notion that transportation and Flagstaff’s remote location will be a significant barrier to attracting meetings and conventions. Many meeting planners are interested in the proposed

project because they believe a key weakness in Flagstaff currently is the lack of enough meeting space and upscale hotel rooms. Some meeting planners indicate that traffic congestion, summer crowds, and the lack of adjacent hotels will be a weakness for the proposed facility. Cold winter weather may also make seasonality an important concern for the project.

Implications of Interviews & Survey Results

Several key factors from the market overview and demand analysis have implications for what level of demand potential exists and what types of events are most suitable for the subject market. Some of the most important factors can be summarized as follows:

- Location will make facility primarily dependent on drive-in local, state, and regional demand;
- The addition of a conference center with significantly more meeting space than existing facilities will address the number one obstacle to attracting more group business to Flagstaff;
- Existing air service levels and location will limit the ability to attract large corporate meetings from Central Arizona and Southern Arizona;
- Existing hotel supply will limit ability to attract large meetings and conventions for upscale groups;
- The addition of a hotel conference center with approximately 250 full-service guestrooms would be attractive for small and medium sized corporate meetings and state association conventions;
- Relatively inexpensive market will be attractive to price-sensitive consumers and organizations such as state associations and SMERF groups, as well as corporate groups in peak season;
- Seasonality is likely to be a major factor in group demand. Meeting planners overwhelmingly view Flagstaff as a summer destination.

HVS concludes there is a substantial amount of statewide demand for meetings and conferences. Key target markets should include state associations, university groups, large government employers located in the area, and small-to-medium sized corporate meetings. Tour and travel groups

may represent additional group demand, especially in the summer and winter. Flagstaff is also positioned as a commercial hub for Northern Arizona. As such, there is a substantial market for local events such as meetings, banquets, assemblies, and social functions.

The success of a new hotel conference center in Flagstaff will depend largely on the ability to attract new event types to the community. Specifically, corporate meetings and state association conventions offer the areas of greatest potential for out-of-town event demand. Therefore, any new facility in Flagstaff will need a substantial amount of banquet and breakout meeting space to serve different functions at these multi-day events. Due to the seasonality of demand, it will also be important to have the ability to host multiple, simultaneous events at the proposed facility.

Any new facility in Flagstaff should be designed to accommodate larger meeting and banquet groups than existing facilities, such as Little America and the Radisson. Furthermore, flexible meeting space will be critical to success because groups indicate a broad range of space requirements. HVS found only limited demand for a fixed-seat amphitheater. However, more meetings rooms or a larger divisible ballroom would increase the subject's capacity to host simultaneous events during peak summer and weekend periods.

Flagstaff has an opportunity to increase its role in the state meetings market based upon the feedback from meeting planners and tourism officials. But it also faces many of the same challenges as other mid-sized markets across the nation. As major metropolitan markets and first-tier destination cities compete for the most prestigious national and regional meetings and conventions, smaller cities have targeted state association events. State association event planners are often compelled to rotate their event locations because members live all across their respective states. Attracting groups from around the state and region are likely to have significant economic impacts as visitors spend money on hotels, meals, and recreation.

HVS makes demand projections based on these key findings in our market research, trends in the industry, event planner interviews and surveys, and our knowledge of comparable projects in other markets.

Figure 7-10 summarizes 35 key evaluation factors that have implications for demand potential of the proposed hotel conference center.

Figure 7-10
Summary Matrix of Demand Indicators

Indicator	Implication for Event Demand			Result / Comment
	High	Medium	Low	
Market Area Factors				
Demographic Trends	★			Growing population & incomes
Local Business Climate		★		Local economy stabilized by government/research sector
Overall Hotel Supply			★	Large supply of limited service; few upscale properties
Facility Rental Rates		★		Wide range of regional competition
Industry Trends				
Industry Supply & Demand Trends			★	Supply growing; demand stable or down
Technology Trends	★			Recommend facility adds state-of-the-art technology
Emerging Industry Trends		★		Travel trends closer to home; travel budgets still conservative
National Economic Trends		★		Labor market lagging; budget deficits; GDP resuming growth
Peer Market Analysis				
Regional Competition			★	Several regional conference centers and resort hotels
Local Competition	★			Limited competition includes hotels and university
Peer Performance		★		Peers mixed; waiting for corporate sector to rebound
Demand Segments				
Historical Demand			★	Flagstaff has not been a meetings/convention destination
Conventions		★		Significant demand among state associations
Meetings/Conferences	★			Corporate, government, and SMERF segments show interest
Banquets	★			Substantial demand in the local market
Training Seminars		★		Moderate demand from institutional clients
Key Informants				
Ability to Attract Attendees		★		Meeting planners give a score slightly above average
Cleanliness of Community		★		Meeting planners give a score slightly above average
Climate	★			Cooler summer temperatures attracts visitors from around AZ
Cultural Activities		★		Grand Canyon and Route 66 are major cultural attractions
Dining & Entertainment		★		Meeting planners give a score slightly above average
Hotel Room Rates		★		Meeting planners expect a discount in Flagstaff
Quality of Hotel Rooms			★	Hotel supply is dominated by discount properties
Perceived Safety	★			Flagstaff receives high marks from meeting planners
Recreational Opportunities	★			Flagstaff receives high marks from meeting planners
Air Service			★	Air lift is very limited
Drive-in Transportation		★		Highway system is good
Survey Response Rate	★			Response rate indicates interest in project
Focus Groups		★		Meeting planners show interest, but are uncommitted
Lost Business Analysis			★	Lost business is minimal; not targeted toward subject property
Recommended Facility Program				
Ability to Service Simultaneous Events		★		Large divisible ballroom is critical
Overall Size of Facility	★			Largest meeting room block in northern Arizona
Hotel Room Count	★			Subject will be the largest hotel in the market area
Hotel Flag		★		Uncertain
Level of Finishes, Amenities, Services	★			Ability to serve upscale conferences; IACC certification

Source: HVS International

Based on 35 key demand indicators, Flagstaff demonstrates potential for growth in overall event demand. In particular, there is substantial potential

for growth in demand for upscale meetings, conferences, and banquets. Twelve (12) of the summarized factors are likely to have positive implications for demand. Sixteen (16) factors are likely to have neutral implications for demand. Only seven (7) factors are likely to have negative implications for demand. Certain negative factors, such as supply and demand trends in the industry and the current state of the national economy, cannot be addressed. But other negative factors, such as the supply of meeting space and the quality and quantity of Flagstaff's hotel supply, could be addressed by the subject project to improve demand potential. Other challenges, such as air service, may be addressed in the future.

Demand Projections

The information revealed in the market overview, peer analysis, lost business reports, interviews and meeting planner surveys indicates that the development of a hotel conference center could generate a modest amount of statewide convention demand and a substantial amount of demand for meetings and banquets. Based on our findings, HVS projects demand potential for the proposed hotel conference center in downtown Flagstaff.

Table 7-8 shows the annual number of events and attendance by event type projected for the subject project. Fiscal years begin in April.

Table 7-8
Demand Projection of Events and Attendance

	2006	2007	2008	2009	2010-2015
Events					
Conventions	2	6	8	10	10
Conferences	10	15	20	20	20
Meetings	600	900	1,100	1,100	1,100
Banquets	50	120	140	140	140
Training Seminars	10	20	30	35	35
Other	5	10	15	15	15
Total Events	677	1,071	1,313	1,320	1,320
Average Attendances					
Conventions	250	260	270	280	280
Conferences	125	125	125	125	125
Meetings	35	35	35	35	35
Banquets	250	250	250	250	250
Training Seminars	50	50	50	50	50
Other	200	200	200	200	200
Annual Attendance					
Conventions	500	1,560	2,160	2,800	2,800
Conferences	1,250	1,875	2,500	2,500	2,500
Meetings	21,000	31,500	38,500	38,500	38,500
Banquets	12,500	30,000	35,000	35,000	35,000
Training Seminars	500	1,000	1,500	1,750	1,750
Other	1,000	2,000	3,000	3,000	3,000
Total Attendance	36,750	67,935	82,660	83,550	83,550

Source: HVS International

The projected events and attendance for fiscal year 2009 (beginning April 2009) represents stabilized demand. The projections assume an increase in overall demand from the opening year, beginning in April 2006, through stabilization, as is typical of most conference centers. Different event types reach their stabilized level of demand more quickly than others. For example, the demand for banquets, which is generated primarily by local businesses and organizations, stabilizes by the second year of operation. But conventions do not reach stabilized demand until the fourth year of operation, mainly because these events are booked further in advance and event planners hesitate to book events in a facility until it establishes a track record of success.

In a stable operating year HVS projects demand potential for approximately 1,320 events. Based on the likely mix of event types at the facility and assumptions about average attendance by event type, total annual attendance is projected to reach approximately 84,000 people in a stable operating year.

Projected Room Nights

HVS estimated the room nights the projected events would generate if the proposed hotel conference center is developed. HVS calculated these room night estimates by multiplying the number of attendees by three factors: (1) the percentage of attendees who require lodging; (2) the average length of stay in the market; and (3) the percentage of events and attendees who are expected to be new to the market on account of the subject facility.

HVS uses the term “induced” room night demand to mean only those room nights that are expected to be new to Flagstaff because of the proposed hotel conference center. This analysis focuses on those overnight visits that would not occur in Flagstaff, but for the development of the proposed hotel conference center.

Projections of induced room night demand will assess attendance by type of event. Assumptions regarding lodging demand vary accordingly. The estimates regarding the percentage of attendees requiring lodging are based on HVS industry knowledge and the experience of comparable facilities. HVS tailored these assumptions specifically for Flagstaff, based on the characteristics of events appropriate for the market and the likelihood that attendees to those events would come from far enough away to require overnight lodging. HVS used information from the surveys and interviews as

well as other industry data to estimate average event length by type of event and used this information as a basis for the average number of room nights by attendee.

Table 7-9 shows HVS assumptions regarding the percentage of attendees requiring lodging and average number of room nights per lodging attendee.

Table 7-9
Percent of Attendees Requiring Lodging

Event Type	% Requiring Lodging	Average Number of Roomnights per Lodging Attendee
Conventions	70%	2.5
Conferences	50%	2.0
Meetings	35%	1.0
Banquets	5%	1.5
Training Seminars	20%	1.0
Other	0%	N/A

Source: HVS International

The majority of lodging demand will derive from meetings, conventions, and conferences. The majority of convention attendees will require lodging because they will be coming from out of town. Most state associations are based in Phoenix and membership is concentrated in the central part of the state. Conferences will also have many attendees from out of town. But many participants would also come from the local market area and would not require paid lodging. Local research and institutional clients are also expected to hold a small number of conferences that would primarily serve local area participants. Although the majority of meetings are expected to serve the local market, it is imperative that the selected operator aggressively markets the subject property to out-of-town meeting groups, especially large corporate clients in other parts of the state. The assumptions for banquets imply that many out-of-town guests stay with friends and relatives or drive in only for the day. Local institutions and corporations will represent the majority of demand for training seminars. But the selected operator is expected to target some out-of-town groups for training seminars. HVS assumes other events, such as civic events, will not generate significant room night demand.

A portion of overnight visitors attending events at the proposed hotel conference center would not have come to Flagstaff, but for the development of the subject property. However, a portion of overnight visitors would have come to Flagstaff anyway. Therefore, HVS makes assumptions about what portion of room nights are expected to be new to the market.

Table 7-10 shows what percentage of room night demand is expected to be new to the Flagstaff market area versus what percentage would derive from other hotels in the market.

Table 7-10
New Room Night Demand for Flagstaff

	From Comp Set	New to Flagstaff
Conventions	0%	100%
Conferences	10%	90%
Meetings	30%	70%
Banquets	80%	20%
Training Seminars	40%	60%
Other	100%	0%

Source: HVS International

Very few statewide or regional conventions currently take place in Flagstaff. Therefore, HVS assumes all room night demand associated with conventions will be new to the market. Similarly for conferences, about 90 percent of room night demand is expected to be new, or induced. Although many meetings and training seminars will not generate room night demand, a majority of those that do are expected to be new business for the Flagstaff market. On the other hand, the majority of banquets that generate room night demand would occur elsewhere in the Flagstaff market if the proposed hotel conference center is not developed.

Table 7-11 shows the resulting projection of induced room nights generated by each event type from the opening fiscal year in 2006/2007 through stabilization in fiscal year 2009/2010.

Table 7-11
Projected Induced Room Nights

Event Type	2006	2007	2008	2009
Conventions	875	2,730	3,780	4,900
Conferences	1,125	1,688	2,250	2,250
Meetings	5,145	7,718	9,433	9,433
Banquets	188	450	525	525
Training Seminars	60	120	180	210
Other	-	-	-	-
Total	7,393	12,705	16,168	17,318

Source: HVS International

In a stable operating year the function space at the subject facility is expected to generate demand for approximately 17,300 new hotel room nights in Flagstaff. Due to the nature of scheduling group events and the assumed ramp-up of event demand, this new hotel demand is expected to stabilize approximately four years after the subject facility opens.

Data from comparable projects in other markets can provide a useful check on HVS projections for induced room nights.

Table 7-12 shows total group room night estimates and induced room night estimates for the four comparable projects reviewed in a previous section of this report.

Table 7-12
Comparison of Data from Comparable Projects

Name of Facility	Total Group Room Nights	Est. Induced Room Nights
The Chattanooga	30,900	17,000
Renaissance Portsmouth	30,300	21,800
Provo Marriott Hotel & Conf. Ctr.	25,300	17,300
Tempe Mission Palms	50,700	21,700
Average of Peers	34,300	19,450
Proposed Grand Flagstaff	23,850	17,318

Source: HVS International

The proposed hotel conference center in Flagstaff is likely to generate a somewhat smaller number of group room nights than the selected comparable properties. Market size, location, facility size, and other

competitive factors imply the subject property will have a somewhat smaller target market than the selected peers. But HVS projections for induced room nights are in the range exhibited by these other properties. This is due to the fact that Flagstaff would have a higher portion of its overall group business specifically because of the proposed conference center.

The number of room nights the proposed hotel conference center will generate is a modest, but significant, increase in the recorded group room demand in Flagstaff hotels. The subject hotel would capture much of the room nights generated by events at the conference center. But some attendees may elect to stay in other area hotels for reasons such as cost, membership rewards, or perceived convenience. Especially due to recent changes in technology, many attendees who participate in events at the conference center may book their rooms independently, instead of relying on the room block established for their event or booking their room through the Flagstaff CVB. As a result, individual hotels may record such room nights as independent business demand rather than group demand.

8. Hotel Supply and Demand Analysis

In the economic principle of supply and demand, price varies directly, but not proportionately, with demand and inversely, but not proportionately, with supply. In the lodging industry, supply is measured by the number of guestrooms available and demand is measured by the number of guestrooms accommodated. The purpose of this section is to investigate current supply and demand trends as indicated by the current competitive market, and set forth a basis for the projection of future supply and demand growth.

Due to its anticipated level of facilities and amenities offered, the proposed subject property will be extensively marketed as a destination conference center. The proposed subject property will rely upon capturing meeting and group demand from corporations and associations based primarily in Phoenix, Arizona. The subject property will compete for these groups with destinations throughout Arizona, including those located in Tucson, Scottsdale, and Phoenix.

Flagstaff as a destination attracts other types of demand that will also be accommodated at the proposed subject property. Due to its location along Interstate 40 and proximate to the Grand Canyon, hotels in Flagstaff accommodate a majority of leisure transient demand, particularly during the peak summer travel months. Additionally, the medical and research facilities, university, and local, state, and federal agencies located in Flagstaff generate significant amounts of commercial transient and meeting and group demand. Therefore, we have focused our analysis on local factors influencing hotel supply and demand but considered a more regional demand base.

Definition of Subject Hotel Market

The subject site is located in the Flagstaff market, which contains a total of 4,600 rooms and 65 lodging facilities, including many aging, unbranded, limited-service facilities with exterior corridors located along historic Route 66. While many of Flagstaff's lodging facilities are old, the proposed subject property is anticipated to compete primarily with the higher-rated full-service properties and, to a lesser extent, with the higher-rated, branded, limited-service properties within Flagstaff. Due to the subject property's conference

center facilities and market orientation, which will need to draw on a demand base that includes a significant number of meeting and group guests, the subject property's competitive set has been expanded to include four full-service hotel and conference center facilities with an additional 691 rooms located in the towns of Prescott and Sedona, destinations similar to Flagstaff, located north of Phoenix, to more fully illustrate the subject's market position and competitive dynamics. Selectively, the proposed subject property's competitive set includes 11 hotels with a total of 1,607 rooms.

Historical Supply and Demand Data

Smith Travel Research (STR) is an independent research firm that compiles data on the lodging industry; the data published by STR is routinely used by typical hotel buyers. HVS International has ordered and analyzed an STR Trends Report with historical supply and demand data for the proposed subject property and its competitors. This information is presented in the following table, along with the marketwide occupancy, average rate, and rooms revenue per available room (RevPAR). Rooms revenue per available room is calculated by multiplying occupancy by average rate, and provides an indication of how well rooms revenue is being maximized.

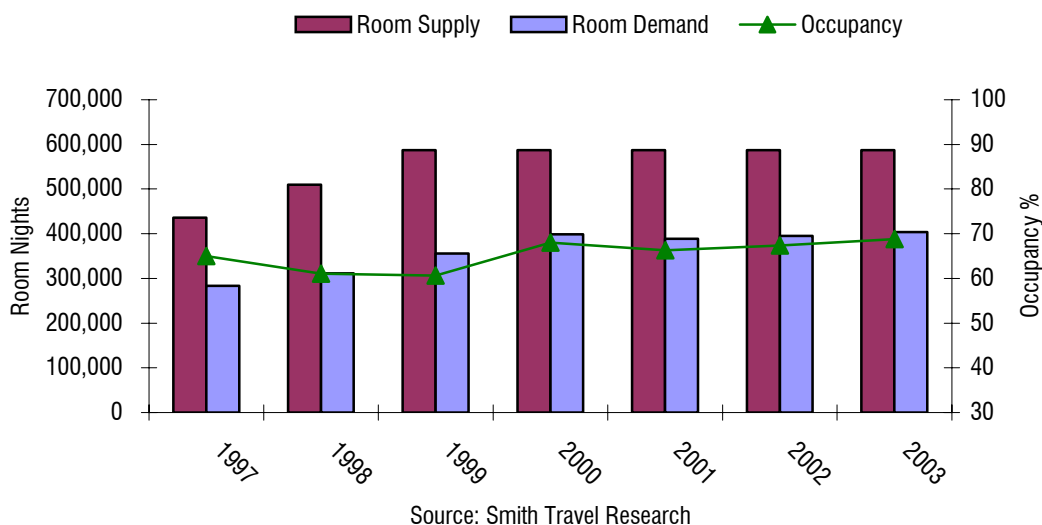
The Flagstaff properties included in the trend report are the Little America, the Radisson Woodlands Hotel, the Embassy Suites, the Hampton Inn, the Hampton Inn & Suites, the Hilton Garden Inn, and the Residence Inn. The competitive set was expanded regionally to include the Hilton Sedona Resort & Spa, the Radisson Poco Diablo, and the Los Abrigados Resort & Spa in Sedona and the Prescott Resort & Conference Center in Prescott.

Table 8-1 Historical Supply and Demand Trends (STR)

Year	Occupied Room Nights	Change	Available Room Nights	Change	Occupancy	Average Rate	Change	RevPAR	Change
1997	283,449	----	436,060	----	65.0 %	\$94.47	----	\$61.41	----
1998	311,169	9.8 %	509,503	16.8 %	61.1	97.70	3.4 %	59.67	(2.8) %
1999	355,510	14.2	586,555	15.1	60.6	84.72	(13.3)	51.35	(13.9)
2000	398,738	12.2	586,555	0.0	68.0	86.63	2.3	58.89	14.7
2001	388,680	(2.5)	586,555	0.0	66.3	91.66	5.8	60.74	3.1
2002	395,028	1.6	586,555	0.0	67.3	93.60	2.1	63.04	3.8
2003	403,586	2.2	586,555	0.0	68.8	95.05	1.5	65.40	3.7
Average Annual									
Compounded Change		6.1 %		5.1 %			0.1 %		1.1 %

Source: Smith Travel Research

Historical Supply and Demand Graph



It is important to note some limitations of the STR data. Hotels are occasionally added to or removed from the sample, and not every property reports data in a consistent and timely manner; these factors can influence the overall quality of the information by skewing the results. These inconsistencies may also cause the STR data to differ from the results of our competitive survey. Nonetheless, STR data provide the best indication of aggregate growth or decline in existing supply and demand, and thus they have been considered in our analysis.

Competitive supply in the proposed subject property's market has not changed since the opening of the 219-room Hilton Sedona Resort & Spa in December of 1998 and the 90-room Hilton Garden Inn in Flagstaff in October of 1997. These properties increased the marketwide supply, measured by available room nights, by roughly 24.0%. Demand also increased as these properties ramped-up; however, their absorption required several years and marketwide occupancy levels reached their nadir in 1999 at 60.6%. Concurrently, average rates decreased by 13.3% in 1999 to \$84.72 as competitive pressures depressed average rates. The new supply was fully absorbed by 2000 as the marketwide occupancy level recorded in that year (68.0%) exceeded the level of 65.0% recorded in 1997 before the additions to supply came on line. In 2001, demand fell slightly; this small decline was notable compared to the severe effects on the lodging and travel industries

caused by waning economic growth and the terrorist attacks in September of that year. In 2002 and 2003, marketwide occupancy levels rose to a peak of 68.8% in 2003. Average rates have grown slightly over that period from \$91.66 in 2001 to \$95.05 in 2003. RevPAR has steadily grown at a moderate rate over the past three years.

Trends in monthly occupancy and average rate are illustrated in the following tables.

Table 8-2 Monthly Occupancy Trends (STR)

Month	1997	1998	1999	2000	2001	2002	2003
January	44.9 %	37.9 %	32.1 %	41.9 %	44.5 %	41.6 %	44.8 %
February	60.3	47.8	46.1	55.8	59.3	58.8	57.8
March	75.5	61.3	59.0	68.6	67.4	69.6	68.0
April	72.7	73.3	60.8	75.9	71.6	71.6	73.9
May	71.9	66.6	61.5	73.7	67.2	73.8	73.1
June	71.4	74.1	69.5	80.4	79.9	79.6	78.1
July	76.0	74.6	76.7	82.4	79.9	81.4	82.9
August	73.7	72.7	74.6	77.0	77.2	77.7	80.4
September	69.2	65.9	67.7	74.4	69.5	68.2	70.8
October	68.6	70.4	71.2	73.1	73.5	76.5	79.1
November	50.5	49.1	57.5	59.6	56.9	58.4	62.2
December	47.2	39.8	49.5	52.3	48.1	50.4	53.9
Annual Occupancy	65.0 %	61.1 %	60.6 %	68.0 %	66.3 %	67.3 %	68.8 %

Source: Smith Travel Research

Table 8-3 Monthly Average Rate Trends (STR)

Month	1997	1998	1999	2000	2001	2002	2003
January	\$75.79	\$83.97	\$76.06	\$70.32	\$74.30	\$77.73	\$80.15
February	82.57	87.36	79.47	74.44	77.05	83.94	84.04
March	95.52	93.88	77.87	82.05	87.30	91.73	89.97
April	100.73	99.91	85.12	89.12	93.36	96.26	96.24
May	101.03	106.56	91.42	93.12	104.99	100.56	103.02
June	97.01	104.96	91.04	91.50	98.98	97.31	99.17
July	93.38	101.05	91.31	90.67	94.08	95.65	98.82
August	97.91	98.71	87.83	89.82	94.50	96.80	98.91
September	94.19	99.70	86.03	91.02	94.33	95.33	97.66
October	98.75	102.16	88.09	90.65	95.84	100.10	102.02
November	96.30	93.40	74.37	80.77	86.86	89.47	90.12
December	89.69	83.04	75.68	81.36	84.00	84.33	86.79
Annual Average Rate	\$94.47	\$97.70	\$84.72	\$86.63	\$91.66	\$93.60	\$95.05

Source: Smith Travel Research

The trends indicate a notable degree of seasonality in demand for lodging accommodations in the proposed subject property's market. Occupancy rates are highest during the summer months of June, July, and August, concurrent with increased summer vacation highway travel. The Grand Canyon is a particularly strong demand generator of transient leisure travelers during the summer months and Flagstaff serves as its southern gateway city. Additionally, the high elevation and temperate weather of the Flagstaff area serve as a welcome respite to the intense desert heat of Phoenix in the summer. Reportedly, a large amount of summer visitation to the market area is generated simply by the need to get out of the oppressive heat of Phoenix. The shoulder seasons of March through May and October and November also experience strong demand characteristics. November through February typically represent the weakest months of the year for hotel demand, as the warm weather of Scottsdale, Phoenix, and Tucson is generally preferable to the colder weather of Flagstaff. Sedona and Prescott generally maintain a stronger base of demand throughout the winter and do not exhibit such volatile occupancy levels. Marketwide average rates vary by \$20 between the peak summer months and the coldest winter months. Generally, Flagstaff lodging properties experience greater seasonal fluctuations than those in Sedona and Prescott.

SUPPLY

An integral component of the supply and demand relationship that has a direct impact on the availability of lodging demand is the current and

anticipated supply of competitive lodging facilities. Due to its anticipated level of facilities and amenities offered, the proposed subject property will be extensively marketed as a destination conference center. The proposed subject property will rely upon capturing meeting and group demand from corporations and associations based primarily in Phoenix, Arizona. The subject property will compete for these groups with destinations throughout Arizona including those located in Tucson, Scottsdale, and Phoenix.

Based on an evaluation of the occupancy, rate structure, market orientation, chain affiliation, location, facilities, amenities, reputation, and quality of the area's hotels, we have identified four properties that are considered primarily competitive with the proposed conference center hotel. Without including the proposed subject property, these primary competitors total 767 rooms. Seven additional lodging facilities are judged to be only secondarily competitive; although the facilities, rate structures, locations, or market orientations of these hotels prevent their inclusion among the primarily competitive supply, they do compete with the proposed subject property to some extent. The room count of each secondary competitor has been weighted to reflect the degree to which it competes with the proposed conference center hotel. The aggregate weighted room count of the secondary competitors is 420 rooms. With 4,600 rooms currently available in the city of Flagstaff market alone, the proposed subject property's competitive set constitutes less than 25% of the total areawide supply.

Primary Competitors

The following tables summarize the important operating characteristics of the primary and secondary competitors. This information was compiled from personal interviews, inspections, lodging directories, and our in-house library of operating data. The tables also set forth each property's penetration factors; penetration is the ratio between a specific hotel's operating results and the corresponding data for the market. If the penetration factor is greater than 100%, the property is performing better than the market as a whole; conversely, if the penetration is less than 100%, the hotel is performing at a level below the marketwide average.

Table 8-4 Primary Competitors and Aggregate Secondary Competitors

Property	Number of Rooms	Estimated Segmentation			Estimated 2001			Estimated 2002			Estimated 2003					
		Commercial	Meeting and Group	Leisure	Occupancy	Average Rate	RevPAR	Occupancy	Average Rate	RevPAR	Weighted Annual Room Count	Occupancy	Average Rate	RevPAR	Occupancy Penetration	Yield Penetration
Little America	246	20 %	40 %	40 %	72.0 %	\$85.00	\$61.20	73.0 %	\$90.00	\$65.70	246	73.0 %	\$92.00	\$67.16	105.4 %	100.2 %
Radisson Woodlands Hotel	183	20	35	45	55.0	77.00	42.35	51.0	76.00	38.76	183	63.0	69.00	43.47	91.0	64.9
Hilton Sedona Resort & Spa	219	10	45	45	68.0	124.00	84.32	73.0	128.00	93.44	219	71.0	138.00	97.98	102.5	146.2
Embassy Suites	119	30	5	65	62.0	94.00	58.28	69.0	90.00	62.10	119	70.0	91.00	63.70	101.1	95.1
Sub-Totals/Averages	767	19 %	35 %	46 %	65.3 %	\$96.32	\$62.85	67.1 %	\$99.26	\$66.63	767	69.6 %	\$100.28	\$69.77	100.5 %	104.1 %
Secondary Competitors	840	18 %	21 %	62 %	67.2 %	\$87.58	\$58.83	68.1 %	\$88.44	\$60.23	420	68.6 %	\$90.28	\$61.95	99.1 %	92.5 %
Totals/Averages	1,607	18 %	30 %	52 %	65.9 %	\$93.17	\$61.43	67.5 %	\$95.40	\$64.37	1,187	69.2 %	\$96.77	\$67.00	100.0 %	100.0 %

Table 8-5 Primary Competitors

Property	Number of Rooms	Year Opened	Meeting Space (SF)	Meeting Space per Room	Ownership Entity	Management Company
Little America	246	1974	13,170	53.5	Sinclair Oil Corporation	Little America Hotels & Resorts
Radisson Woodlands Hotel	183	1990	6,000	32.8	Uniwell Corporation	The Hotel Group LLC
Hilton Sedona Resort & Spa	219	1998	20,500	93.6	Mass Mutual Financial Group	Hilton Hotels Corporation
Embassy Suites	119	1987	1,400	11.8	Remington Hotels Corporation	Ashford Hospitality Trust
Totals/Averages	767		41,070	53.5		

Our survey of the primarily competitive hotels in the Flagstaff and Sedona market shows a positive trend in occupancy levels with average rates exhibiting more modest growth. The Hilton Sedona Resort & Spa was the average rate leader in the market and Little America was the leader in occupancy level in 2003. The market demand has a leisure orientation with this segment comprising 52% of total lodging demand in 2003. The meeting and group segment comprised 30% of the total, followed by the commercial segment. In 2003, the primary competitors achieved an estimated overall occupancy of 69.6% at an estimated average rate of \$100.28, yielding a RevPAR result of \$69.77.

The primary competitors are shown in the following map. Note that the Hilton Resort & Spa is located roughly 40 miles south of the subject site and is not shown. Each primary competitor was inspected and evaluated. Descriptions of our findings are presented on the following pages.

Map of the Competition





Little America

Location: 2515 East Butler Avenue
Flagstaff, Arizona

Table 8-6 Estimated Historical Operating Statistics

	Wtd. Annual Room Count	Occupancy	Average Rate	RevPAR	Occupancy Penetration	Yield Penetration
2001	246	72 %	\$85	\$61	109.2 %	99.6 %
2002	246	73	90	66	108.2	102.1
2003	246	73	92	67	105.4	100.2

The Little America is located at exit 198 along I-40, roughly 2.0 miles west of the subject site and downtown Flagstaff. The property opened in June 1974 on 500 acres planted with Ponderosa pine. The 246 guestrooms are contained in four, two-story lodges. The oversized guestrooms are decorated in one of four different color schemes and are furnished with either two queen-size beds or one king-size bed. Additionally, the guestrooms feature separate seating areas, marble sinks and vanities, and 31" televisions. The property features three food and beverage outlets and offers room service. It has a 6,300-square-foot ballroom and 13,170 total square feet of meeting space as well as several outdoor lawns and pavilions suitable for hosting social events, weather permitting.

The Little America is one of four similar properties located throughout the western United States. Like the others, this property has never undergone a complete renovation; however, at the time of inspection the property was clean and well-maintained. According to property management, a team of craftsmen are employed to continuously refurbish selected areas of the Little America hotels. The Little America enjoys a high degree of repeat leisure business, which is estimated to comprise 40% of total accommodated demand. Additionally, the property's meeting facilities account for another 40% of accommodated demand for predominantly social, military, educational, religious, fraternal (SMERF) and association-related events. Commercial business is estimated to account for the remaining 20% of accommodated demand. The property also has a heated outdoor pool, hot tub, children's playground, a two-mile recreational trail, and a large gift shop.

Due to the property's location, full-service orientation, supply of meeting space, and estimated average rate we consider the Little America to be directly competitive with the proposed subject property.



Radisson Woodlands Hotel

Location: 1175 West Route 66
Flagstaff, Arizona

Table 8-7 Estimated Historical Operating Statistics

	Wtd. Annual Room Count	Occupancy	Average Rate	RevPAR	Occupancy Penetration	Yield Penetration
2001	183	55 %	\$77	\$42	83.4 %	68.9 %
2002	183	51	76	39	75.6	60.2
2003	183	63	69	43	91.0	64.9

The Radisson Woodlands Hotel is located roughly two miles west of the subject site, along Route 66. The property opened in 1975 as a Best Western Hotel and was converted to the Radisson brand in 1999. Since that time, there have been no major renovations at the property, although a complete guestroom refurbishment is planned for 2005. The property has three food and beverage outlets and roughly 6,000 square feet of meeting space, including a 3,900 square foot ballroom that is divisible in three. The Radisson features an indoor whirlpool and an outdoor pool as well as a fitness room and a gift shop. The 183 guestrooms are furnished with either one king bed or two queen beds and were in fair condition at the time of our inspection.

Based on conversations with property management, we estimate that the Radisson Woodlands accommodates roughly 45% of its demand from the leisure market segment, 35% demand from the meeting and group segment, and the remainder from the leisure segment. Due to the property's location, full-service orientation, supply of meeting space, and brand affiliation we consider the Radisson Woodlands to be directly competitive with the proposed subject property.



Hilton Sedona Resort & Spa

Location: 90 Ridge Trail Drive
Sedona, Arizona

Table 8-8 Estimated Historical Operating Statistics

	Wtd. Annual Room Count	Occupancy	Average Rate	RevPAR	Occupancy Penetration	Yield Penetration
2001	219	68 %	\$124	\$84	103.1 %	137.3 %
2002	219	73	128	93	108.2	145.2
2003	219	71	138	98	102.5	146.2

The Hilton Sedona Resort & Spa is located roughly 40 miles south of the subject site in the town of Sedona. The 219-room property features a full-service spa, three swimming pools, two food and beverage outlets, and 20,500 square feet of meeting and function space, including a roughly 5,000-square-foot ballroom. Additionally, guests of the Hilton Sedona Resort & Spa have preferred access to the Stone Ridge Golf Course, located proximate to the property.

The property originally opened in 1998 as a Doubletree hotel and was briefly marketed as a timeshare resort. The guestrooms are spacious, and each is equipped with a gas fireplace, wet bar, microwave, a patio or balcony, separate seating area, and two televisions. In 2001, Hilton was brought in to operate the property again as a transient hotel. In 2003, property

management completed a \$3.5 million renovation of the spa facilities. At the time of our inspection, the property appeared to be in very good condition.

According to property management, the Hilton Sedona Resort & Spa is a popular site for social gatherings, particularly weddings, as well as a destination for corporate retreats, training, and team building. Therefore, we estimate that the meeting and group segment is 45% of total accommodated demand at the property. Leisure is the other primary component of accommodated demand, estimated at 45%, due to the attraction of the soaring Red Rocks formations.

Due to the property's full-service orientation, large inventory of meeting space, brand affiliation, and location similar to Flagstaff relative to Phoenix, we consider the Hilton Sedona Resort & Sap to be directly competitive with the proposed subject property.



Embassy Suites

Location: 700 South Milton Road
Flagstaff, Arizona

Table 8-9 Estimated Historical Operating Statistics

	Wtd. Annual Room Count	Occupancy	Average Rate	RevPAR	Occupancy Penetration	Yield Penetration
2001	119	62 %	\$94	\$58	94.0 %	94.9 %
2002	119	69	90	62	102.3	96.5
2003	119	70	91	64	101.1	95.1

The Embassy Suites is located roughly one mile southwest of the subject site along the primary access road between Flagstaff and the interstate highways. The property opened in June 1988 and after seven years of operation as a Quality Inn was converted to an Embassy Suites. Today the property offers 119 two-room guest suites and roughly 1,400 square feet of meeting space configured in two meeting rooms. The property also has an outdoor pool and whirlpool and a breakfast-only restaurant; cocktails are served nightly in the lobby. At the time of our inspection, the facilities appeared to be in good condition. In October 2003, the property was sold by Felcor Lodging Trust to Ashford Hospitality Trust. According to property management, the new owners are planning a \$1.0 million renovation of the lobby and softgoods refurbishment of the guestrooms. Additionally, the property's primary

meeting room, measuring ± 725 square feet, will be converted into a bar. The most recent capital improvements at the property were new carpets installed in the corridors and guestrooms in May 2003.

According to property management, the property accommodates 95% transient demand, primarily from the leisure segment, and a minimal amount of meeting and group demand due to the property's limited meeting facilities. However, due to the property's affiliation with Hilton Hotels Corporation and its rewards programs, the Embassy Suites is reportedly popular with higher-rated, commercial transient business travelers.

Due to the property's location, rate structure, market orientation, and brand affiliation we consider the Embassy Suites to be directly competitive with the proposed subject property.

**Secondary
Competitors**

The secondary competitors were deemed less competitive due to differences in location, amenities, facilities, rate structure, or market orientation, among other things. Considering these factors, the consultants assigned each secondary competitor a percentage of competitiveness that expresses the extent to which it competes with the proposed subject property. The room count of each of the secondary competitors, as weighted, as well as other pertinent data, is included in the following chart.

Table 8-10 Secondary Competitors

Property	Number of Rooms	Estimated Segmentation			Total Competitive Level	Estimated 2001			Estimated 2002			Estimated 2003			
		Commercial	Meeting and Group	Leisure		Occupancy	Average Rate	RevPAR	Occupancy	Average Rate	RevPAR	Weighted Annual Room Count	Occupancy	Average Rate	RevPAR
Radisson Poco Diablo	137	10 %	25 %	65 %	50 %	65 %	\$103.00	\$66.95	70.0 %	\$97.00	\$67.90	69	73.0 %	\$102.00	\$74.46
Los Abridados Resort & Spa	175	5	20	75	50	65	120.00	78.00	66.0	125.00	82.50	88	67.0	128.00	85.76
Hampton Inn	50	25	10	65	50	82	69.00	56.58	81.0	75.00	60.75	25	78.0	75.00	58.50
Hampton Inn & Suites	126	25	10	65	50	72	77.00	55.44	73.0	74.00	54.02	63	74.0	75.00	55.50
Hilton Garden Inn	90	25	15	60	50	79	67.00	52.93	74.0	71.00	52.54	45	74.0	70.00	51.80
Residence Inn	102	30	20	50	50	74	81.00	59.94	80.0	77.00	61.60	51	74.0	78.00	57.72
Prescott Resort & Conference	160	15	40	45	50	52	71.00	36.92	50.0	75.00	37.50	80	53.0	75.00	39.75
Totals/Averages	840	18 %	21 %	62 %	50 %	67.2 %	\$87.58	\$58.83	68.1 %	\$88.44	\$60.23	420	68.6 %	\$90.28	\$61.95

A cluster of secondarily competitive hotels is located roughly 35 miles southwest of the proposed subject property's site, in the town of Sedona, set among the spectacular natural scenery of the Red Rocks formations. This cluster includes the Radisson Poco Diablo Hotel and the Los Abridados Resort & Spa.

The 137-room **Radisson Poco Diablo** features a nine-hole, par 3 golf course, an outdoor pool and two whirlpool spas, a fitness center offering massage services, and tennis and basketball courts. The property has two food and beverage outlets and roughly 5,500 square feet of meeting space, including a 3,300-square-foot ballroom that is divisible into four spaces. The property was initially operated as an independent hotel and was converted to the Radisson brand in 2000. In March 2001 a \$3.0 million renovation of the lobby and public areas and refurbishment of the guestrooms was completed and, at the time of our inspection, the property appeared to be in good condition. Due to the property's location, inventory of meeting space, facilities and amenities, and market orientation, we consider the Radisson Poco Diablo to be 50% competitive with the proposed subject property.

The **Los Abridados Resort & Spa** is located roughly 35 miles southwest of the proposed subject property in Sedona, Arizona. The 175-room resort is situated on 22 acres along the banks of a creek with impressive views of the Red Rocks formations and is one of three timeshare properties owned by ILX Resorts Incorporated in the Sedona area. Guestrooms are appointed with wet bars, balconies, and separate living areas. Many guestrooms have fireplaces and whirlpools. This property is the largest and most centrally located of the ILX-owned properties, with the largest inventory of meeting space and the highest quality amenities. According to competitive property managers, Los Abridados is competitive in the social meetings, special events, and SMERF market segments. Due to the property's location, market orientation, and rate structure we consider the Los Abridados Resort & Spa to be 50% competitive with the proposed subject property.

The largest cluster of secondarily competitive hotels is located in the Flagstaff area and includes the Hampton Inn, the Hampton Inn & Suites, the Hilton Garden Inn, and the Residence Inn. These properties are considered limited-service, or focused-service, properties that are expected to secondarily compete with the proposed subject property for the lower-rated transient business in the market area. We consider them to be competitive with the proposed subject property due to the market orientation of their brands, their rate structures, and their locations proximate to the subject site. However, due

to their lack of a significant inventory of meeting space or a sales and marketing staff dedicated to group sales we consider these properties to be 50% competitive with the proposed subject property.

The **Hampton Inn** is located roughly 3.5 miles northeast of the subject site, accessed by Old Highway 66 and exit 201 of I-40. This 50-room property opened in May 1995, and features an indoor pool and whirlpool, a complimentary continental breakfast, and free cable television. The 126-room **Hampton Inn & Suites**, which opened in February 1998, is located roughly 2.0 miles southwest of the subject site near the crossroads of I-17 and I-40, proximate to the Northern Arizona University campus. The one-bedroom suites offer a fully equipped kitchen, living room with sofa bed, dining area, and a private bedroom. The property features an indoor pool and whirlpool, an exercise room, and small meeting facilities. A continental breakfast is complimentary, and the property is proximate to a multitude of food and beverage outlets and retail shopping. The 90-room **Hilton Garden Inn** is located proximate to the Hampton Inn & Suites and opened in October 1997. The Hilton Garden Inn offers a breakfast café and 24-hour pantry store, a business center, indoor pool, whirlpool, and sauna. Guestrooms are equipped with a refrigerator, microwave oven, and coffee maker. The **Residence Inn** opened in 1991 and features 102 guest suites with full kitchens, separate seating areas, and king-sized beds. Many guestrooms have fireplaces. A continental breakfast is complimentary, as is a weekday evening social hour, and the property also has a fully-equipped fitness room, heated pool and whirlpool, and outdoor sport court. The Residence Inn is located roughly 4.5 miles east of the subject site, accessed by exit 201 of I-40, and accommodates predominantly extended stay guests as well as commercial and leisure transient demand. The property has one small meeting room and, as such, does not accommodate a significant amount of meeting and group demand.

Finally, the **Prescott Resort & Conference Center** is located roughly 85 miles southwest of the subject site in the town of Prescott, Arizona. The 160-room property is located directly next to Bucky's Casino and across the street from the Yavapai Casino. Each guestroom has a refrigerator, coffee maker, balcony, and cable television. Hospitality suites are available to host receptions and small meetings in addition to the property's inventory of roughly 14,000 square feet of flexible meeting and event space, including a 6,440-square-foot ballroom divisible into four spaces. The property has two food and beverage outlets on-site and is proximate to several others. The property offers a full array of recreational amenities including swimming, tennis, racquetball, and weight training on-site. The health club and salon offer whirlpool, sauna,

massage, and beauty treatments. We consider the Prescott Resort & Conference Center to be 50% competitive with the proposed subject property due to its meeting and event facilities, location, and market orientation.

Supply Changes

It is important to consider any proposed hotels that may have an impact on the proposed subject property's operating performance in the future. Based on our fieldwork in the market and our discussions with local hotel operators, developers, and government officials, we have not identified any properties besides the subject property that are proposed or under development in the subject market area.

While we have taken reasonable steps to investigate proposed hotel projects and their status, due to the nature of real estate development, it is impossible to determine with certainty every hotel that will be opened in the future, or what their marketing strategies and effect in the market will be. However, future improvement in market conditions will raise the risk of increased competition. The consultants' forthcoming forecast of stabilized occupancy and average rate are intended to reflect such risk.

Demand Analysis Using Market Segmentation

For the purpose of demand analysis, the overall market is divided into individual segments based on the nature of travel. Market segmentation is a useful procedure because individual classifications often exhibit unique characteristics in terms of growth potential, seasonality of demand, average length of stay, double occupancy, facility requirements, price sensitivity, and so forth. By quantifying the room night demand by market segment and analyzing the characteristics of each segment, the demand for transient accommodations can be projected. Based on our fieldwork, area analysis, and knowledge of the local lodging market, we estimate the 2003 distribution of accommodated room night demand as follows.

Table 8-11 Accommodated Room Night Demand

Market Segment	Marketwide	
	Accommodated Demand	Percentage of Total
Commercial	54,743	18 %
Meeting and Group	90,031	30
Leisure	155,201	52
Total	299,975	100 %

Marketwide accommodated demand is composed of 52% leisure demand and 30% meeting and group demand. Commercial demand currently is estimated to compose 18% of the total accommodated demand. The proposed subject property is forecast to predominantly accommodate meeting and group demand. The commercial and leisure segments are forecast to compose lesser proportions of total accommodated demand at the proposed subject property than are currently accommodated marketwide.

Using the distribution of accommodated hotel demand as a starting point, we will analyze the characteristics of each market segment to determine future trends in room night demand.

Commercial Segment

The commercial segment consists of individual businesspeople who are visiting various firms in the proposed subject property's market. This demand is strongest Monday through Thursday nights, declines significantly on Friday and Saturday, and increases somewhat on Sunday. The typical length of stay for commercial guests ranges from one to three days, and the rate of double occupancy is a low 1.2 to 1.3 people per room. Commercial demand is relatively constant throughout the year, although some declines are noticeable in late December and during other holiday periods.

Commercial demand in the proposed subject property's market is generated by a wide variety of corporations, with the corporate offices of local manufacturers exhibiting some dominance. Additionally, the Flagstaff Medical Center (FMC) and the United States Geological Survey (USGS) are important drivers of commercial demand; however, FMC aggressively renegotiates rates each year, and because of volume has a very low negotiated rate. Similarly, the USGS generally negotiates the government per diem rate of \$55 in the winter and \$67 in the summer for its visitors.

All of the economic and demographic data presented earlier have some influence on commercial lodging demand. The trends that have the most direct correlation are changes in financial, insurance, and real estate (FIRE); service; wholesale trade; total employment; and airport passenger counts. Smith Travel Research estimates that overall lodging demand in the local market increased at an average annually compounded rate of 3.2% from 1999 through 2003. Considering these trends, we project 3.0% growth in commercial demand in 2004, 2005, and 2006; slowing to 2.5% growth in 2007, 2.0% in 2008, and stabilizing at 1.0% in 2009.

Meeting and Group Segment

The meeting and group market includes meetings, seminars, conventions, trade association shows, and similar gatherings of 10 or more people. Peak meeting and convention demand typically occurs in the spring and fall. Because of vacations, the summer months represent the slowest period for this market segment, while winter demand varies. Although there are numerous classifications within the meeting and group segment, the primary categories considered in this analysis are corporate groups, associations, and SMERF groups.

Corporate groups are one of the most profitable components of this segment, because they exhibit limited price sensitivity and they often sponsor banquets and other events that generate revenue for the host hotel. In the subject property's market, most corporate group activity is generated by the same major employers that contribute high-volume corporate accounts. This demand may take the form of training programs, sales meetings, division conferences, and similar events with a business purpose. Corporate groups generally meet during the workweek, thus generating lodging demand on Monday through Thursday nights. The average length of stay is two to four days, although training groups may stay six nights or more. Double-occupancy rates in this category typically range from 1.0 to 1.5.

Association demand is generally divided on a geographical basis: the most common categories are national, regional, and state associations. Depending on their nature, these associations may be more rate sensitive than commercial groups. This is particularly true when members are not reimbursed by their employers but must pay to attend (for example, guestroom and conference fees). The scheduling pattern of associations also depends on the nature of the group. Professional associations and/or those supported by members' employers often meet on weekdays, while other associations prefer to hold events on weekends.

The SMERF market consists of groups that are social, military, educational, religious, or fraternal in nature. Examples include family or military reunions, youth groups, and fraternal organizations such as the Knights of Columbus. These groups are extremely budget conscious, and have a strong preference for weekend and summer meeting times, when rates are generally lowest. Typically, groups such as this have a high double-occupancy rate of 2.0 to 2.5, and the length of stay is relatively short (one to three nights). Most hotel operators use this type of demand to bolster occupancy during off-peak times of the month and year, when other demand sources are limited.

In projecting meeting and group demand in the proposed subject property's market, we have considered all of the data sources applicable to the commercial segment, as well as trends in convention activity and leisure travel and the results of our survey of meeting planners. It appears that the meeting and group market in Flagstaff is being underserved by the existing supply of meeting facilities. Corporations are reportedly meeting on-site or in inconvenient locations with inadequate facilities. Therefore, the construction of higher-quality meeting space in flexible arrangements located in downtown Flagstaff is expected to encourage an increased utilization rate of meeting facilities in the market area. Given these factors, we estimate that meeting and group demand will increase by 3.0% in 2004, 2005, and 2006. In 2007, we forecast growth in meeting and group demand to moderate to 2.0% and, we forecast growth of 1.0% thereafter.

Leisure Segment

The leisure market segment consists of individuals and families who are spending time in the area or passing through en route to other destinations. Their travel purposes may include sightseeing, recreation, visiting friends and relatives, or numerous other non-business activities. Leisure demand is strongest Friday and Saturday nights and all week during holiday periods and the summer months. These peak periods are negatively correlated with commercial visitation, underscoring the stabilizing effect of capturing weekend and summer tourist travel. The typical length of stay ranges from one to four days, depending on the destination and travel purpose, and the rate of double occupancy typically ranges from 1.8 to 2.5 people per room.

Future leisure demand is related to the overall economic health of the region and the nation. Trends showing changes in state and regional unemployment and disposable personal income often have a strong correlation to non-commercial visitation. Of the economic and demographic data presented earlier in this report, trends in retail sales, retail sector employment, total employment, and air traffic counts tend to have the strongest influence on leisure demand. Additionally, the Flagstaff market has a large pool of leisure demand that is currently being served by non-competitive, exterior-corridor, unbranded limited-service lodging facilities. As the proposed subject property enters the market and competes for commercial and meeting and group business with the existing facilities, we forecast that leisure demand that was previously accommodated at some of the poorer-quality lodging facilities in the market will migrate to the branded properties. Although generally lower-rated, leisure demand does pay a higher rate than the government per diem or negotiated corporate rates and should not erode marketwide average rate attainment. Based on our analysis of these indicators, we project growth in

the leisure segment at a rate of 2.5% in 2004, 3.5% in 2005, and increasing to 6.0% in 2006 as the proposed subject property comes on-line. This upward migration of leisure demand is expected to moderate in 2007 to register 4.0% growth and decrease further to 2.0% growth in 2008. We forecast 1.0% growth as the subject property reaches stabilization in 2009.

Conclusion

The purpose of segmenting the lodging market is to define each major type of demand, identify customer characteristics, and estimate future growth trends. We have identified three segments as constituting the proposed subject property's lodging market. Various types of economic and demographic data were then evaluated to determine their propensity to reflect changes in hotel demand. Based on this procedure, we have forecast the following annual base growth rates for each segment.

Table 8-12 Market Segment Growth Rates

Market Segment	Annual Growth Rate						
	2004	2005	2006	2007	2008	2009	2010
Commercial	3.0 %	3.0 %	3.0 %	2.5 %	2.0 %	1.0 %	1.0 %
Meeting and Group	3.0	3.0	3.0	2.0	1.0	1.0	1.0
Leisure	2.5	3.5	6.0	4.0	2.0	1.0	1.0
Base Demand Growth	2.7 %	3.3 %	4.6 %	3.1 %	1.7 %	1.0 %	1.0 %

These growth rates will be used to forecast changes in lodging demand.

Induced Demand

Induced demand represents the additional room nights that are expected to be attracted to the market following the introduction of a new demand generator. Situations that can result in induced demand include the opening of a new manufacturing plant, the expansion of a convention center, or the addition of a new hotel with a distinct chain affiliation or unique facilities. In this analysis, induced demand is projected based on the consultants' opinion of the potential absorption of the proposed subject property. The number of occupied room nights induced by the new hotel rooms is derived from an estimated occupancy buildup for the hotel from its date of opening through an estimated stabilized year.

The following table summarizes our estimate of induced demand.

Table 8-13 Induced Demand Room Nights

Market Segment	Induced Room Nights				
	2006	2007	2008	2009	2010
Commercial	2,156	3,194	3,513	3,833	3,833
Meeting and Group	6,775	11,292	16,562	18,068	18,068
Leisure	1,540	2,852	3,137	3,422	3,422
Total	10,471	17,338	23,212	25,322	25,322

Induced meeting and group demand is forecast to grow from roughly 6,800 room nights in 2006 to 18,000 room nights in 2009, the stabilized year of operation. We forecast a minimal amount of induced demand in the commercial and leisure segments.

Forecast of Marketwide Occupancy

Based upon a review of the market dynamics in the proposed subject property's competitive environment, we have forecast growth rates for each market segment. We have also analyzed the potential for demand to be induced in the future. In the following table, total demand is then divided by the forecast of market supply, rendering an overall estimate of areawide occupancy. Thus, the forecast of marketwide occupancy is calculated as follows:

Table 8-14 Forecast of Market Occupancy

	2003	2004	2005	2006	2007	2008	2009	2010
Commercial								
Base Demand	54,743	56,386	58,077	59,820	61,315	62,541	63,167	63,798
Induced Demand		0	0	2,156	3,194	3,513	3,833	3,833
Total Demand		56,386	58,077	61,975	64,509	66,054	66,999	67,631
Growth Rate		3.0 %	3.0 %	6.7 %	4.1 %	2.4 %	1.4 %	0.9 %
Meeting and Group								
Base Demand	90,031	92,732	95,514	98,379	100,347	101,350	102,364	103,387
Induced Demand		0	0	6,775	11,292	16,562	18,068	18,068
Total Demand		92,732	95,514	105,155	111,639	117,912	120,431	121,455
Growth Rate		3.0 %	3.0 %	10.1 %	6.2 %	5.6 %	2.1 %	0.8 %
Leisure								
Base Demand	155,201	159,081	164,649	174,528	181,509	185,139	186,990	188,860
Induced Demand		0	0	1,540	2,852	3,137	3,422	3,422
Total Demand		159,081	164,649	176,068	184,360	188,276	190,412	192,282
Growth Rate		2.5 %	3.5 %	6.9 %	4.7 %	2.1 %	1.1 %	1.0 %
Totals								
Base Demand	299,975	308,199	318,240	332,727	343,171	349,031	352,521	356,046
Induced Demand		0	0	10,471	17,338	23,212	25,322	25,322
Total Accommodated Demand		308,199	318,240	343,197	360,508	372,242	377,843	381,368
Overall Demand Growth		2.7 %	3.3 %	7.8 %	5.0 %	3.3 %	1.5 %	0.9 %
Market Mix								
Commercial	18.2 %	18.3 %	18.2 %	18.1 %	17.9 %	17.7 %	17.7 %	17.7 %
Meeting and Group	30.0	30.1	30.0	30.6	31.0	31.7	31.9	31.8
Leisure	51.7	51.6	51.7	51.3	51.1	50.6	50.4	50.4
Existing Hotel Supply	1,187	1,187	1,187	1,188	1,187	1,187	1,187	1,187
Proposed Hotels								
Proposed Conference Center Hotel ¹				187	250	250	250	250
Available Rooms per Night	433,255	433,255	433,255	502,005	524,505	524,505	524,505	524,505
Nights per Year	365	365	365	365	365	365	365	365
Total Supply	1,187	1,187	1,187	1,375	1,437	1,437	1,437	1,437
Rooms Supply Growth	—	0.0 %	0.0 %	15.9 %	4.5 %	0.0 %	0.0 %	0.0 %
Marketwide Occupancy	69.2 %	71.1 %	73.5 %	68.4 %	68.7 %	71.0 %	72.0 %	72.7 %

¹ Opening in April 2006 of the 100% competitive, 250-room proposed conference center hotel

The addition of the proposed subject property will induce a significant amount of meeting and group demand. We anticipate that the market will quickly absorb the proposed subject property and forecast marketwide occupancy to reach the low-70% range within three years of the proposed subject property's opening.

9. Projection of Occupancy

Along with average rate results, the occupancy levels achieved by a hotel are the foundation of the property's financial performance and market value. Most of a lodging facility's other revenue sources (such as food, beverages, and telephone income) are driven by the number of guests, and many expense levels also vary with occupancy. Consequently, a well-documented forecast of occupancy is critical to the valuation process.

To a certain degree, occupancy attainment can be manipulated by management. For example, hotel operators may choose to lower rates in an effort to maximize occupancy. Our forecasts reflect an operating strategy that we believe would be implemented by a typical, professional hotel management team to achieve an optimal mix of occupancy and average rate.

Penetration Rate Analysis

The proposed subject property's forecasted market share and occupancy levels are based upon its anticipated competitive position within the market, as quantified by its penetration rate. The penetration rate is the ratio of a property's market share to its fair share.

In this equation, market share represents that portion of total market demand accommodated by a property and fair share represents the subject hotel's portion of the total supply (calculated as the subject's room count divided by the total supply of the market at large).

If a property with a fair share of 5% is capturing 5% of the market demand in a given year, then its occupancy will equal the marketwide occupancy, and its penetration rate will equal 100% ($5\% \div 5\% = 100\%$). If the same property achieves a market share in excess of its fair share, then its occupancy will be greater than the marketwide occupancy, and its penetration rate will be greater than 100%. For example, if a property's fair share is 5% and its market share is 7%, then its penetration rate is 140% ($7\% \div 5\% = 140\%$). Conversely, if the property captures less than its fair share, then its occupancy will be below the marketwide average, and its penetration rate will be less than 100%.

Penetration rates can be calculated for each market segment captured by a given property, and for the property as a whole. For example, a property's leisure segment penetration can be determined by dividing the property's leisure room nights captured (property's total room nights captured multiplied by property's leisure segment percentage) by the hotel's fair share of total areawide leisure demand (the property's fair share percentage multiplied by the market's total leisure room night demand). Simplifying the formula, a hotel's market share percentage divided by its fair share percentage equals its market penetration. In essence, a penetration rate above 100% in a certain market segment indicates that the hotel is capturing more than its fair share of that source of demand, while a penetration rate below 100% indicates that a hotel is capturing less than its fair share of demand. A penetration rate of 100% indicates that the hotel is capturing its pro-rata share of the market segment's room night demand.

Historical Penetration Rates by Market Segment

In the following table, the penetration rates attained by the primary competitors and the aggregate secondary competitors are set forth for each segment for the base year, 2003. The results are used as a basis for comparison with the proposed subject property, as well as our forecast of penetration rates for the subject and each competitive hotel into the future.

Table 9-1 Historical Penetration Rates

Property	Commercial	Meeting and Group	Leisure	Overall
Little America	116 %	141 %	82 %	105 %
Radisson Woodlands Hotel	100	106	79	91
Hilton Sedona Resort & Spa	56	154	89	103
Embassy Suites	166	17	127	101
Secondary Competition	95	69	118	99

Historically, commercial and leisure transient demand segments have been highly competitive within the Flagstaff lodging market due to an overabundance of aging, lower-rated, limited-service, exterior-corridor properties lining the interstate and state highways that suppress the average daily rates that would otherwise be attainable by full-service, interior-corridor properties such as the Little America, Radisson Woodlands Hotel, and Embassy Suites. The Embassy Suites is the market leader in commercial-

segment occupancy penetration due to its brand reputation and favorable location along Route 89A between downtown Flagstaff and the interstate highway interchange. The Little America is the overall leader in occupancy penetration due to its well-established customer base, extensive facilities, and strong representation in each of the market segments.

Whereas, the Little America and Radisson Woodlands Hotel are the market leaders that accommodate the vast majority of meeting and group demand generated within Flagstaff, these hotels compete with hotels in Prescott and Sedona for drive-in business from Phoenix. The Hilton Sedona Resort and Spa is the overall leader in meeting and group penetration due to its modern and attractive facilities and the added benefits of the Hilton sales, marketing, and reservation systems. The Prescott Resort and Conference Center offers a lower-rated alternative for meeting and group demand as well as casino gaming entertainment.

Forecast of Subject Property's Penetration

Because the supply and demand balance for the competitive market is dynamic, particularly in relation to proposed new hotel supply entering the competitive market, there is a circular relationship between the penetration factors of each hotel in the market. The performance of individual new hotels has a direct effect upon the aggregate performance of the market, and consequently upon the calculated penetration factor for each hotel in each market segment. The same is true when the performance of existing hotels changes, either positively (following a refurbishment, for example) or negatively (when a poorly maintained or marketed hotel loses market share).

A hotel's penetration factor is calculated as its achieved market share of demand divided by its fair share of demand. Thus, if one hotel's penetration performance increases, thereby increasing its achieved market share, this leaves less demand available in the market for the other hotels to capture and the penetration performance of one or more of those other hotels consequently declines (other things remaining equal). This type of market share adjustment takes place every time there is a change in supply, or a change in the relative penetration performance of one or more hotels in the competitive market.

Our projections of penetration, demand capture, and occupancy performance for the subject property account for these types of adjustments to market share within the defined competitive market. Consequently, the actual penetration factors applicable to the subject property and its competitors for each market segment in each projection year may vary somewhat from the

penetration factors delineated in the previous tables. Based on the preceding analyses, the subject property's occupancy forecast is set forth as follows, with the adjusted projected penetration rates used as a basis for calculating the amount of captured market demand.

Table 9-2 Forecast of Subject Property's Occupancy

Market Segment	2006	2007	2008	2009	2010
Commercial					
Demand	61,975	64,509	66,054	66,999	67,631
Market Share	12.4 %	17.4 %	18.1 %	18.8 %	18.8 %
Capture	7,688	11,223	11,962	12,602	12,721
Penetration	91 %	100 %	104 %	108 %	108 %
Meeting and Group					
Demand	105,155	111,639	117,912	120,431	121,455
Market Share	17.8 %	23.9 %	25.2 %	26.4 %	26.4 %
Capture	18,717	26,718	29,726	31,850	32,121
Penetration	131 %	138 %	145 %	152 %	152 %
Leisure					
Demand	176,068	184,360	188,276	190,412	192,282
Market Share	3.1 %	5.9 %	7.8 %	7.8 %	7.8 %
Capture	5,371	10,956	14,629	14,795	14,940
Penetration	22 %	34 %	45 %	45 %	45 %
Total Room Nights Captured	31,776	48,897	56,318	59,248	59,783
Available Room Nights	68,250	91,250	91,250	91,250	91,250
Subject Occupancy	47 %	54 %	62 %	65 %	66 %
Marketwide Available Room Nights	502,005	524,505	524,505	524,505	524,505
Fair Share	14 %	17 %	17 %	17 %	17 %
Marketwide Occupied Room Nights	343,197	360,508	372,242	377,843	381,368
Market Share	9 %	14 %	15 %	16 %	16 %
Marketwide Occupancy	68 %	69 %	71 %	72 %	73 %
Total Penetration	68 %	78 %	87 %	90 %	90 %

Overall, the proposed subject property is forecast to increase its total penetration level from 68% in the first year of operation to 90% in the stabilized year. This performance will be largely dependent upon property management's ability to induce meeting and group demand into the market, as the subject is forecast to garner a 152% meeting and group occupancy

penetration level in the stabilized year. The proposed subject property is forecast to capture a percentage of commercial demand greater than its fair share, as the proposed facilities plan is designed to fill an upscale niche currently unmet by the existing lodging supply in Flagstaff. However, the relatively high room rates of the subject property are forecast to hinder the effective capture of more price-sensitive demand.

Subject Property's Market Segmentation

The following table summarizes the subject property's projected market segmentation.

Table 9-3 Subject Property's Market Segmentation

	2006	2007	2008	2009	2010
Commercial	24 %	23 %	21 %	21 %	21 %
Meeting and Group	59	55	53	54	54
Leisure	17	22	26	25	25
Total	100 %	100 %	100 %	100 %	100 %

Upon the proposed subject property's forecasted opening in 2006, meeting and group demand is expected to comprise 59% of the subject's total accommodated demand. Much of this demand is forecast to be induced to the market by the construction of the subject property's premium conference facilities and by the advance sales and marketing efforts of Benchmark Hospitality, the proposed management company. As the proposed subject property ramps up to full operation, leisure transient demand is forecast to comprise a greater proportion of total accommodated demand as effective distribution channels are established and greater awareness of the proposed subject property is achieved through sales and marketing efforts and customer referrals. While commercial demand is forecast to comprise a decreasing percentage of total accommodated demand, the gross number of commercial accommodated room nights is forecast to grow, but at a lesser rate than the other segments.

Forecast of Subject Property's Occupancy

Based on the preceding analysis, the following forecast of occupancy results. Dividing the total number of room nights captured by the subject property's annual number of available room nights (calculated as 250 x 365) produces the projected occupancy percentage.

Table 9-4 Subject Property's Occupancy Forecast

	2006	2007	2008	2009	2010
Total Room Nights Captured	31,776	48,897	56,318	59,248	59,783
Available Room Nights	68,250	91,250	91,250	91,250	91,250
Subject Occupancy	46.6 %	53.6 %	61.7 %	64.9 %	65.5 %
Rounded	47 %	54 %	62 %	65 %	66 %

We have chosen to use a stabilized occupancy of 65%. The stabilized occupancy is intended to reflect the anticipated results of the property over its remaining economic life, given any and all changes in the life cycle of the hotel. Thus, the stabilized occupancy excludes from consideration any abnormal relationship between supply and demand, as well as any nonrecurring conditions that may result in unusually high or low occupancies. Although the subject property may operate at occupancies above this stabilized level, we believe it equally possible for new competition and temporary economic downturns to force the occupancy below this selected point of stability.

These projections have been adjusted to reflect fiscal years beginning April 1, 2006, corresponding to the first projection year for the subject property's forecast of income and expense.

Table 9-5 Forecast of Occupancy

Year	Subject Occupancy
2006/07	48 %
2007/08	56
2008/09	63
2009/10	65

10. Average Rate Analysis

One of the most important considerations in estimating the value of a lodging facility is a supportable forecast of its attainable average rate, which is more formally defined as the average rate per occupied room. Average rate can be calculated by dividing the total rooms revenue achieved during a specified period by the number of rooms sold during the same period. The projected average rate and the anticipated occupancy percentage are used to forecast rooms revenue, which in turn provides the basis for estimating most other income and expense categories.

Competitive Position

Although the average rate analysis presented here follows the occupancy projection, these two statistics are highly correlated; in reality, one cannot project occupancy without making specific assumptions regarding average rate. This relationship is best illustrated by revenue per available room (RevPAR), which reflects a property's ability to maximize rooms revenue.

The market for transient commercial and leisure accommodations in Flagstaff is traditionally price-sensitive. Area property managers have indicated that the unwillingness of many guests to pay premium rates for lodging is a major reason why the market lacks high-quality, full-service lodging facilities. Sedona is a higher-rated destination due to the resort nature of the town, and to the views and recreation opportunities afforded by the Red Rocks formations.

The following table summarizes the historical average rate and the RevPAR of the subject property's competitors.

Table 10-1 Base Year Average Rate and RevPAR of the Subject's Primary Competitors

Property	Estimated 2003 Average Room Rate	Rooms Revenue Per Available Room
Little America	\$92.00	\$67.16
Radisson Woodlands Hotel	69.00	43.47
Hilton Sedona Resort & Spa	138.00	97.98
Embassy Suites	91.00	63.70
Average	\$100.28	\$69.77

As illustrated in the preceding table, average room rates for the competitive full-service hotels in the market area in 2003 ranged from \$69 to \$138. The Hilton Sedona Resort & Spa achieved the highest average daily rate and RevPAR among the direct competitors due to its resort location, quality of facilities, brand affiliation, and customer base. The Radisson Woodlands Hotel in Flagstaff recorded the lowest average rate and RevPAR among the direct competitors in 2003. The proposed subject property is forecast to be the rate leader in the Flagstaff market, although remaining behind the Hilton Sedona Resort & Spa, due to the expected quality of construction, brand identity, and market orientation.

CMP Rates

As mentioned, one of the distinguishing characteristics of conference center facilities is their offering of Complete Meeting Packages. The CMP rate includes guestroom accommodations, three meals per day, refreshments, conference services, and basic A/V equipment. The offering of a CMP rate benefits the conference center and conference attendees alike. Unlike à-la-carte pricing at traditional hotels, the CMP rate often represents significant savings for conference attendees, while entitling the subject property to all of their patrons' food and beverage sales. This bundling of services enables conference centers to capture high revenues per guest while offering a discount on the cost of services to the entity using the facilities.

An integral component of an evaluation of the operation of a conference center lodging facility is to determine the assessment of what percentage of the complete meeting package rate should be allocated to rooms revenue, food and beverage revenue, and conference services revenue. A study released in 2003 prepared by PKF Consulting and the IACC entitled "Trends in the Conference Center Industry" provides a range of percentages upon which to base these allocations. Per this study, the following chart presents

the allocation of complete meeting package rates for resort- and executive-oriented facilities.

Table 10-2 Allocation of CMP Rates—Resort and Executive Facilities

Allocation	Resort and Executive Facilities	
	Average Rates	% of Total
CMP Rooms	\$151 - 179	58 - 62 %
CMP Food & Beverage	64 - 78	25 - 27
CMP Conference Services	24 - 26	8 - 10
Total CMP Average Rate	\$246 - 291	100 %

Source: PKF Consulting & International Association of Conference Centers

The allocation of CMP revenues differs between operators. Generally, one or more allocated components of the CMP rate are fixed and the remaining components vary depending upon the specific CMP rates negotiated by the sales and marketing team. By keeping the CMP allocation to certain departments fixed throughout the year, property management is able to more effectively monitor income and expenses across all operating departments. We assume some portion of the group and meeting demand will be CMP demand. This is inherently included in our forecast.

Market Segmentation Method

In the market segmentation method, average room rate is projected by individual market segment. This is the preferred method for forecasting average rate, based on the operational and marketing practices of hotel operators. Consistent with hotel management's tracking of historical average rates by market segment and their own budgeting methods, segmentation of demand and average rate allows for yield management resulting in the maximization of room revenue.

Based upon the segmented average room rates achieved by the competitive hotels, as well as our discussions with area general managers, we have estimated the average room rate that the subject would have achieved in 2003, by segment, had the hotel been operational and stabilized at that time. Each market segment's average rate is projected through the stabilized year based upon the annual rate of change anticipated for that market segment's rate. For each forecast year, the segmented average rate is multiplied by the number of occupied rooms previously projected to be captured in that segment; this results in a forecast of total rooms revenue by market segment.

The segmented rooms revenue is summed, resulting in the total rooms revenue. Dividing the total rooms revenue by the total number of occupied rooms results in the overall weighted average room rate.

The proposed subject property is forecast to achieve a strong average daily rate as it will be built within downtown Flagstaff and will feature the most modern guestrooms and most extensive meeting and group facilities in the market. This expected base of commercial demand is forecast to enable the proposed subject property to increase its commercial rate by 5.0% in 2006, 4.0% in 2007, and 3.0% in 2008 through stabilization in 2009.

The addition of high-quality meeting and banquet space in Flagstaff is forecast to induce a substantial amount of new demand. Some groups that outgrew existing facilities in Flagstaff are expected to return, and other groups that were previously underserved by inferior facilities will have the opportunity to trade up to superior-quality facilities. These events will enable the proposed subject property to increase the average rate in the meeting and group segment by 4.5% in 2006, 4.0% in 2007, and 3.0% in 2008 through stabilization in 2009.

Average daily rates in the leisure market segment are forecast to grow by 3.0% in 2006 through stabilization in 2009 as leisure demand fills in the gaps left by commercial and meeting and group demand. Leisure rates will grow at a slightly lower rate than average rates in the meeting and group market segment because leisure travelers tend to be more rate sensitive, and because the high-quality meeting and banqueting space is of little utility to such travelers.

The following table identifies the growth rates that have been applied to each segmented average rate through the stabilized year. As a context for the average rate growth factors, note that we have applied a base underlying inflation rate of 2.0% in 2004 and 2005, and 3.0% throughout the remainder of our projection.

We anticipate that the subject will be required to build up to its stabilized average rate by providing discounts in the first two years of operation, which we have estimated at 10.0% in year one and 5.0% in year two.

Table 10-3 Subject Property's Average Rate Forecast

	2006	2007	2008	2009	2010
Commercial					
Average Rate Growth	5.0 %	4.0 %	3.0 %	3.0 %	3.0 %
Captured Room Nights	7,688	11,223	11,962	12,602	12,721
Rooms Revenue	\$1,347,710	\$2,046,025	\$2,246,257	\$2,437,466	\$2,534,260
Average Rate	\$175.30	\$182.31	\$187.78	\$193.41	\$199.21
Meeting and Group					
Average Rate Growth	4.5 %	4.0 %	3.0 %	3.0 %	3.0 %
Captured Room Nights	18,717	26,718	29,726	31,850	32,121
Rooms Revenue	\$2,990,315	\$4,439,221	\$5,087,315	\$5,614,314	\$5,831,896
Average Rate	\$159.76	\$166.15	\$171.14	\$176.27	\$181.56
Leisure					
Average Rate Growth	3.0 %	3.0 %	3.0 %	3.0 %	3.0 %
Captured Room Nights	5,371	10,956	14,629	14,795	14,940
Rooms Revenue	\$674,888	\$1,418,131	\$1,950,292	\$2,031,597	\$2,113,094
Average Rate	\$125.66	\$129.43	\$133.32	\$137.32	\$141.44
Total					
Average Rate Growth	-	2.5 %	2.0 %	3.2 %	3.0 %
Captured Room Nights	31,776	48,897	56,318	59,248	59,783
Rooms Revenue	\$5,012,913	\$7,903,377	\$9,283,864	\$10,083,378	\$10,479,250
Average Rate (Before Discount)	\$157.76	\$161.63	\$164.85	\$170.19	\$175.29
Discount	10.0 %	5.0 %	0.0 %	0.0 %	0.0 %
Average Rate After Discount	142.84	154.31	166.17	171.45	176.59
Average Rate in Base Year Dollars	\$133.30	\$139.80	\$146.16	\$146.41	\$146.41

For the purposes of this analysis, we have used 2009 as the stabilized year for average rate. The stabilized average daily rate deflated to current dollars equates to \$146.41. Compared to the subject property's anticipated first-year average daily rate, deflated to current-year dollars, of \$133.30, our forecast indicated real rate growth of \$13.11 through the stabilized year.

Similar to the analysis of the subject's occupancy projections, the forecast of average rate represents fiscal years beginning April 1, 2006. Based upon the preceding analysis, the following table sets forth our "fiscalized" forecast of the subject property's occupancy, average rate, and RevPAR.

Table 10-4 Forecast of Occupancy, Average Rate, and RevPAR

Year	Occupancy	Average Rate		RevPAR	% Change
		Before Discount	% Change		
2006/07	48 %	\$158.71	--	\$76.64	--
2007/08	56	162.43	2.3 %	90.29	17.8 %
2008/09	63	166.17	2.3	103.87	15.0
2009/10	65	171.45	3.2	111.57	7.4

11. Financial Operations

The forecast of income and expense is expressed in current dollars for each year. The stabilized year is intended to reflect the anticipated operating results of the property over its remaining economic life, given any or all applicable stages of build-up, plateau, and decline in the life cycle of the hotel. Thus, income and expense estimates from the stabilized year forward exclude from consideration any abnormal relationship between supply and demand, as well as any nonrecurring conditions that may result in unusual revenues or expenses. The 10-year period reflects the typical holding period of large real estate assets such as hotels. In addition, the 10-year time frame provides for the stabilization of income streams and comparison of yields with alternate types of real estate. The forecast income streams reflect the future benefits of owning specific rights in income-producing real estate.

STR *HOST Report*

In order to project future income and expense for the proposed subject property, we have reviewed composite income and expense statements from the Smith Travel Research *HOST Report*. For the purposes of this assignment, we chose criteria that best describe characteristics of the proposed subject property in a general way: full-service, urban, upscale, 150-300 rooms, and the West South Central region of the United States. The results are shown in the following tables.

Table 11-1 Comparable Operating Data—STR *HOST* Report

		Urban			Upscale		150-300 rooms			West South Central		
Occupancy		63.8%			63.9%		62.2%			64.2%		
Rooms		405			243		216			307		
Average Rate		\$149.94			\$109.83		\$109.85			\$111.32		
REVENUE	%	PAR	POR	%	PAR	POR	%	PAR	POR	%	PAR	POR
Rooms	63.9%	\$36,489	\$149.94	65.0%	\$25,402	\$109.83	64.7%	\$24,667	\$109.85	65.8%	\$26,056	\$111.32
Food	20.2%	\$11,536	\$47.40	19.4%	\$7,576	\$32.76	19.1%	\$7,294	\$32.48	19.1%	\$7,547	\$32.24
Beverage	5.4%	\$3,058	\$12.57	4.9%	\$1,921	\$8.30	5.2%	\$1,975	\$8.80	4.3%	\$1,684	\$7.20
Other Food & Beverage	3.8%	\$2,150	\$8.83	4.1%	\$1,589	\$6.87	3.7%	\$1,424	\$6.34	4.0%	\$1,574	\$6.72
Telephone	2.0%	\$1,146	\$4.71	1.5%	\$571	\$2.47	1.5%	\$582	\$2.59	1.7%	\$670	\$2.86
Minor Operated Departments	2.4%	\$1,351	\$5.55	3.4%	\$1,342	\$5.80	4.2%	\$1,606	\$7.15	3.3%	\$1,297	\$5.54
Rentals & Other Income	2.3%	\$1,394	\$5.72	1.7%	\$671	\$2.90	1.6%	\$543	\$2.56	1.8%	\$779	\$3.33
Total Revenue	100.0%	\$57,124	\$234.72	100.0%	\$39,072	\$168.93	100.0%	\$38,091	\$169.77	100.0%	\$39,607	\$169.21
DEPARTMENTAL EXPENSES												
Rooms	26.8%	\$9,762	\$40.11	26.4%	\$6,707	\$29.00	26.0%	\$6,425	\$28.61	22.9%	\$5,966	\$25.49
Food & Beverage	77.9%	\$13,051	\$53.62	77.6%	\$8,603	\$37.20	78.3%	\$8,377	\$37.31	73.9%	\$7,987	\$34.12
Telephone	56.6%	\$649	\$2.67	68.3%	\$390	\$1.69	62.5%	\$364	\$1.62	65.0%	\$435	\$1.86
Other Departmental Expenses	2.0%	\$1,139	\$4.68	3.0%	\$1,171	\$5.07	3.5%	\$1,312	\$5.84	2.4%	\$955	\$4.08
Total Departmental Expenses	43.1%	\$24,601	\$101.08	43.2%	\$16,871	\$72.96	43.2%	\$16,478	\$73.38	38.7%	\$15,343	\$65.55
Total Departmental Profit	56.9%	\$32,523	\$133.64	56.8%	\$22,201	\$95.97	56.8%	\$21,613	\$96.39	61.3%	\$24,264	\$103.66
UNDISTRIBUTED OPERATING EXPENSES												
Administrative & General	8.0%	\$4,559	\$18.73	8.8%	\$3,450	\$14.92	9.4%	\$3,585	\$15.96	8.5%	\$3,357	\$14.34
Marketing	6.4%	\$3,677	\$15.11	6.9%	\$2,705	\$11.69	7.4%	\$2,803	\$12.48	6.8%	\$2,691	\$11.50
Franchise Fees	0.3%	\$166	\$0.68	0.8%	\$309	\$1.34	1.1%	\$407	\$1.81	0.6%	\$233	\$1.00
Energy	3.6%	\$2,034	\$8.36	4.0%	\$1,563	\$6.76	4.3%	\$1,629	\$7.26	3.9%	\$1,540	\$6.58
Property Operations & Maintenance	4.6%	\$2,643	\$10.86	5.1%	\$2,004	\$8.67	5.4%	\$2,040	\$9.09	4.9%	\$1,947	\$8.32
Total Undistributed Operating Expenses	22.9%	\$13,079	\$53.74	25.6%	\$10,031	\$43.38	27.6%	\$10,464	\$46.60	24.7%	\$9,768	\$41.74
GROSS OPERATING PROFIT	34.3%	\$19,610	\$80.58	31.9%	\$12,479	\$53.93	30.4%	\$11,586	\$51.60	37.2%	\$14,729	\$62.92
Management Fees	3.2%	\$1,808	\$7.43	3.0%	\$1,165	\$5.04	2.9%	\$1,110	\$4.94	3.6%	\$1,443	\$6.16
INCOME BEFORE FIXED CHARGES	31.1%	\$17,802	\$73.15	28.9%	\$11,314	\$48.89	27.5%	\$10,476	\$46.66	33.6%	\$13,286	\$56.76
Property Taxes	4.2%	\$2,396	\$9.84	3.0%	\$1,179	\$5.10	3.0%	\$1,141	\$5.08	3.1%	\$1,218	\$5.20
Insurance	1.0%	\$571	\$2.34	1.1%	\$432	\$1.87	1.2%	\$456	\$2.03	1.0%	\$389	\$1.66
Reserve for Replacement	1.9%	\$1,109	\$4.56	2.3%	\$908	\$3.93	2.1%	\$801	\$3.57	2.1%	\$825	\$3.52
AMOUNT AVAILABLE FOR DEBT SERVICE & OTHER FIXED CHARGES	24.0%	\$13,726	\$56.41	22.5%	\$8,795	\$37.99	21.2%	\$8,078	\$35.98	27.4%	\$10,854	\$46.38

Source: Smith Travel Research

Table 11-2 Comparable Operating Data—STR *HOST* Report

	Aggregate Averages of Comparables				Ranges of Comparables			
Occupancy	63.5%				62.2% - 64.2%			
Rooms	293				216 - 405			
Average Rate	\$120.24				\$109.83 - \$149.94			
REVENUE	%	PAR	POR	%	PAR	POR		
Rooms	64.9%	\$28,154	\$120.24	63.9% - 65.8%	\$24,667 - \$36,489	\$109.83 - \$149.94		
Food	19.5%	\$8,488	\$36.22	19.1% - 20.2%	\$7,294 - \$11,536	\$32.24 - \$47.40		
Beverage	5.0%	\$2,160	\$9.22	4.3% - 5.4%	\$1,684 - \$3,058	\$7.20 - \$12.57		
Other Food & Beverage	3.9%	\$1,684	\$7.19	3.7% - 4.1%	\$1,424 - \$2,150	\$6.34 - \$8.83		
Telephone	1.7%	\$742	\$3.16	1.5% - 2.0%	\$571 - \$1,146	\$2.47 - \$4.71		
Minor Operated Departments	3.3%	\$1,399	\$6.01	2.4% - 4.2%	\$1,297 - \$1,606	\$5.54 - \$7.15		
Rentals & Other Income	1.9%	\$847	\$3.63	1.6% - 2.3%	\$543 - \$1,394	\$2.56 - \$5.72		
Total Revenue	100.0%	\$43,474	\$185.66	100.0% - 100.0%	\$38,091 - \$57,124	\$168.93 - \$234.72		
DEPARTMENTAL EXPENSES								
Rooms	25.5%	\$7,215	\$30.80	22.9% - 26.8%	\$5,966 - \$9,762	\$25.49 - \$40.11		
Food & Beverage	76.9%	\$9,505	\$40.56	73.9% - 78.3%	\$7,987 - \$13,051	\$34.12 - \$53.62		
Telephone	63.1%	\$460	\$1.96	56.6% - 68.3%	\$364 - \$649	\$1.62 - \$2.67		
Other Departmental Expenses	2.7%	\$1,144	\$4.92	2.0% - 3.5%	\$955 - \$1,312	\$4.08 - \$5.84		
Total Departmental Expenses	42.1%	\$18,323	\$78.24	38.7% - 43.2%	\$15,343 - \$24,601	\$65.55 - \$101.08		
Total Departmental Profit	58.0%	\$25,150	\$107.42	56.8% - 61.3%	\$21,613 - \$32,523	\$95.97 - \$133.64		
UNDISTRIBUTED OPERATING EXPENSES								
Administrative & General	8.7%	\$3,738	\$15.99	8.0% - 9.4%	\$3,357 - \$4,559	\$14.34 - \$18.73		
Marketing	6.9%	\$2,969	\$12.70	6.4% - 7.4%	\$2,691 - \$3,677	\$11.50 - \$15.11		
Franchise Fees	0.7%	\$279	\$1.21	0.3% - 1.1%	\$166 - \$407	\$0.68 - \$1.81		
Energy	4.0%	\$1,692	\$7.24	3.6% - 4.3%	\$1,540 - \$2,034	\$6.58 - \$8.36		
Property Operations & Maintenance	5.0%	\$2,159	\$9.24	4.6% - 5.4%	\$1,947 - \$2,643	\$8.32 - \$10.86		
Total Undistributed Operating Expenses	25.2%	\$10,836	\$46.37	22.9% - 27.6%	\$9,768 - \$13,079	\$41.74 - \$53.74		
GROSS OPERATING PROFIT	33.5%	\$14,601	\$62.26	30.4% - 37.2%	\$11,586 - \$19,610	\$51.60 - \$80.58		
Management Fees	3.2%	\$1,382	\$5.89	2.9% - 3.6%	\$1,110 - \$1,808	\$4.94 - \$7.43		
INCOME BEFORE FIXED CHARGES	30.3%	\$13,220	\$56.37	27.5% - 33.6%	\$10,476 - \$17,802	\$46.66 - \$73.15		
Property Taxes	3.3%	\$1,484	\$6.31	3.0% - 4.2%	\$1,141 - \$2,396	\$5.08 - \$9.84		
Insurance	1.1%	\$462	\$1.98	1.0% - 1.2%	\$389 - \$571	\$1.66 - \$2.34		
Reserve for Replacement	2.1%	\$911	\$3.90	1.9% - 2.3%	\$801 - \$1,109	\$3.52 - \$4.56		
AMOUNT AVAILABLE FOR DEBT SERVICE & OTHER FIXED CHARGES	23.8%	\$10,363	\$44.19	21.2% - 27.4%	\$8,078 - \$13,726	\$35.98 - \$56.41		

Source: Smith Travel Research

Comparable Operating Statements

As a measure of potential performance, we have reviewed operating statements from comparable properties to provide an additional gauge by which to assess the subject's future performance; the three following charts present these operating statements derived from HVS International's database of hotel income and expense statements. These historical income and expense statements will be used as benchmarks in our forthcoming forecast of income and expense.

The comparable hotel properties One, Two, and Three are each full-service hotels located within the state of Arizona. Each property is of a similar size compared to the proposed subject property and each derives greater than 25% of its total revenues from food and beverage operations. The comparable hotel statements Four, Five, and Six are conference center hotels located on the outskirts of major metropolitan areas within the United States. Two of these comparable conference center properties are unbranded, as is the proposed subject property, and each of these properties derives significant other income by providing conference services.

The fourth chart presents revenue and expense ratios for various conference center facilities, including all conference centers combined, resort conference centers, and executive conference centers. These revenue and expense ratios were obtained from the 2003 publication, *Trends in the Conference Center Industry*, produced by PKF Consulting and the International Association of Conference Centers. We believe that the comparable statements and the conference center operating ratios can provide an enhanced portrayal of the subject property's potential performance.

Table 11-3 Comparable Operating Data—Percentage of Revenue

	Comp 1	Comp 2	Comp 3	Comp 4	Comp 5	Comp 6
Year:	2003	2002	2002	2002	2002	2002
Number of Rooms:	~270	~340	~320	~240	~400	~380
Occupied Rooms:	72,000	74,000	72,000	41,000	100,000	77,000
Days Open:	365	365	365	365	365	365
Occupancy:	73.0%	60.0%	62.0%	47.0%	69.0%	55.0%
Average Rate:	\$139.00	\$99.00	\$118.00	\$137.00	\$136.00	\$129.00
RevPAR:	\$101.00	\$59.00	\$73.00	\$64.00	\$94.00	\$71.00
REVENUE						
Rooms	66.3 %	54.4 %	50.8 %	51.6 %	47.8 %	39.6 %
Food	30.7	34.8	27.8	25.8	39.4	28.0
Beverage	0.0	4.0	5.2	7.4	3.8	8.6
Telephone	1.1	2.2	0.8	0.9	1.1	1.0
Other Income	1.9	4.6	15.4	14.2	7.9	22.8
Total	100.0	100.0	100.0	100.0	100.0	100.0
DEPARTMENTAL EXPENSES*						
Rooms	23.2	27.1	22.3	22.0	24.8	22.9
Food & Beverage	61.6	71.3	85.1	103.0	63.2	90.1
Telephone	62.3	45.1	143.7	106.9	53.7	69.1
Other Income	22.6	41.1	55.4	74.6	66.5	55.2
Total	35.4	42.4	44.6	49.6	42.6	47.6
DEPARTMENTAL INCOME	64.6	57.6	55.4	50.4	57.4	52.4
OPERATING EXPENSES						
Administrative & General	11.0	10.5	8.1	10.0	6.8	7.9
Marketing	8.2	7.1	7.7	10.0	4.3	7.2
Franchise Fee	0.0	1.0	2.4	0.0	2.0	0.0
Property Operations & Maintenance	4.3	5.2	6.3	8.2	4.7	3.9
Energy	3.3	4.0	4.9	4.9	3.2	3.7
Total	26.8	28.0	29.4	33.2	21.0	22.7
HOUSE PROFIT	37.8	29.6	26.0	17.2	36.4	29.7

* Departmental expense ratios are expressed as a percentage of departmental revenues

Table 11-4 Comparable Operating Data—Per Occupied Room

	Comp 1	Comp 2	Comp 3	Comp 4	Comp 5	Comp 6
Year:	2003	2002	2002	2002	2002	2002
Number of Rooms:	~270	~340	~320	~240	~400	~380
Occupied Rooms:	72,000	74,000	72,000	41,000	100,000	77,000
Days Open:	365	365	365	365	365	365
Occupancy:	73.0%	60.0%	62.0%	47.0%	69.0%	55.0%
Average Rate:	\$139.00	\$99.00	\$118.00	\$137.00	\$136.00	\$129.00
RevPAR:	\$101.00	\$59.00	\$73.00	\$64.00	\$94.00	\$71.00
REVENUE						
Rooms	\$138.77	\$99.45	\$117.58	\$136.66	\$135.70	\$128.88
Food	64.36	63.51	64.36	68.28	111.71	91.19
Beverage	0.00	7.30	12.09	19.52	10.76	27.92
Telephone	2.26	3.97	1.88	2.47	3.15	3.34
Other Income	3.95	8.47	35.65	37.70	22.46	74.34
Total	209.34	182.70	231.56	264.64	283.78	325.67
DEPARTMENTAL EXPENSES						
Rooms	32.24	26.99	26.18	30.09	33.67	29.47
Food & Beverage	39.64	45.26	54.76	70.31	70.64	82.13
Telephone	1.41	1.79	2.70	2.64	1.69	2.31
Other Income	0.89	3.48	19.74	28.11	14.93	41.06
Total	74.19	77.52	103.38	131.16	120.93	154.96
DEPARTMENTAL INCOME	135.16	105.18	128.18	133.48	162.85	170.71
OPERATING EXPENSES						
Administrative & General	23.01	19.19	18.75	26.59	19.44	25.86
Marketing	17.20	13.04	17.82	26.40	12.30	23.47
Franchise Fee	0.00	1.91	5.53	0.00	5.78	0.00
Property Operations & Maintenance	8.92	9.56	14.63	21.80	13.21	12.59
Energy	6.90	7.40	11.30	12.97	8.96	11.93
Total	56.04	51.10	68.03	87.76	59.68	73.85
HOUSE PROFIT	79.12	54.08	60.16	45.73	103.17	96.86

Table 11-5 Comparable Operating Data—Per Available Room

	Comp 1	Comp 2	Comp 3	Comp 4	Comp 5	Comp 6
Year:	2003	2002	2002	2002	2002	2002
Number of Rooms:	~270	~340	~320	~240	~400	~380
Occupied Rooms:	72,000	74,000	72,000	41,000	100,000	77,000
Days Open:	365	365	365	365	365	365
Occupancy:	73.0%	60.0%	62.0%	47.0%	69.0%	55.0%
Average Rate:	\$139.00	\$99.00	\$118.00	\$137.00	\$136.00	\$129.00
RevPAR:	\$101.00	\$59.00	\$73.00	\$64.00	\$94.00	\$71.00
REVENUE						
Rooms	\$36,807	\$21,626	\$26,541	\$23,372	\$34,359	\$25,708
Food	17,070	13,810	14,528	11,678	28,284	18,190
Beverage	0	1,588	2,730	3,339	2,724	5,570
Telephone	600	863	425	423	797	667
Other Income	1,048	1,842	8,047	6,448	5,686	14,828
Total	55,526	39,728	52,270	45,259	71,851	64,964
DEPARTMENTAL EXPENSES						
Rooms	8,552	5,868	5,909	5,146	8,524	5,878
Food & Beverage	10,515	9,842	12,362	12,025	17,886	16,383
Telephone	374	389	610	452	428	461
Other Income	237	757	4,456	4,808	3,780	8,190
Total	19,678	16,857	23,336	22,431	30,618	30,911
DEPARTMENTAL INCOME	35,848	22,871	28,934	22,828	41,233	34,052
OPERATING EXPENSES						
Administrative & General	6,104	4,173	4,233	4,548	4,922	5,159
Marketing	4,563	2,836	4,022	4,515	3,114	4,682
Franchise Fee	0	415	1,248	0	1,463	0
Property Operations & Maintenance	2,367	2,079	3,302	3,728	3,344	2,510
Energy	1,830	1,608	2,550	2,218	2,268	2,380
Total	14,863	11,111	15,355	15,008	15,111	14,732
HOUSE PROFIT	20,985	11,760	13,579	7,820	26,122	19,320

Table 11-6 Conference Center Operating Ratios—Percentage of Revenue*

	Type of Conference Center		
	All Properties	Executive Properties	Resort Properties
REVENUE			
Rooms	41.7 %	44.2 %	37.3 %
Food	28.7	28.2	28.5
Beverage	4.9	6.0	6.2
Telephone	1.1	1.3	1.2
Conference Services	13.7	16.5	10.4
Minor Operating Departments	3.7	1.4	6.9
Total	100.0	100.0	100.0
DEPARTMENTAL EXPENSES**			
Rooms	25.1	24.6	24.0
Food and Beverage	74.2	75.5	70.1
Telephone	75.9	63.9	66.0
Conference Services	42.4	38.5	54.1
Minor Operating Departments	54.1	53.9	48.5
Total	46.2	45.1	47.0
DEPARTMENTAL INCOME	53.8	54.9	53.0
OPERATING EXPENSES			
Administrative & General	9.5	10.5	8.7
Marketing	6.8	7.1	7.7
Property Operations & Maintenance	6.1	5.8	4.5
Energy	3.6	3.8	3.5
Total	26.0	27.3	24.4
HOUSE PROFIT	27.8	27.6	28.6
Base Management Fee	2.1	2.7	2.3
INCOME BEFORE OTHER FIXED CHARGES	25.7	24.9	26.3

* Totals may not add up due to the use of median statistics

** Departmental expense ratios are expressed as a percentage of departmental revenues

Source: PKF Consulting & International Association of Conference Centers

Departmental income among these comparable properties ranged between 50.4% and 64.6% of total revenue. The house profit of the comparables ranged from 17.2% of total revenue to 37.8%, which indicates the volatility of this asset class as well as their potential for high profitability. The conference center study indicated a more narrow departmental income range from 53.0% to 54.9% of total revenue and house profit range from 27.6% to 28.6%.

Premise of Forecast

The forecast of income and expense is intended to reflect the consultants' subjective estimate of how a typical buyer would project the subject property's future operating results.

**Fixed and Variable
Component Analysis**

HVS International uses a fixed and variable component model to project a lodging facility's revenue and expense levels. This model is based on the premise that hotel revenues and expenses have one component that is fixed and another that varies directly with occupancy and facility usage. A projection can be made by taking a known level of revenue or expense and calculating its fixed and variable components. The fixed component is then increased in tandem with the underlying rate of inflation, while the variable component is adjusted for a specific measure of volume such as total revenue.

The following table illustrates the revenue and expense categories that can be projected using this fixed and variable component model. These percentages show the portion of each category that is typically fixed and variable; the middle column describes the basis for calculating the percentage of variability, while the last column sets forth the fixed percentage that has been utilized in this valuation.

Table 11-7 Range of Fixed and Variable Ratios

Category	Percent Fixed	Percent Variable	Index of Variability	Fixed Ratio
Revenues				
Food	25 - 50 %	50 - 75 %	Occupancy	10 %
Beverage	0 - 30	70 - 100	Food Revenue	0
Telephone	10 - 40	60 - 90	Occupancy	10
Conference Services	30 - 60	40 - 70	Occupancy	70
Other Income	30 - 60	40 - 70	Occupancy	70
Departmental Expenses				
Rooms	50 - 70	30 - 50	Occupancy	60
Food & Beverage	35 - 60	40 - 65	Food & Beverage Revenue	55
Telephone	40 - 60	40 - 60	Telephone Revenue	60
Conference Services	40 - 60	40 - 60	Conference Services Revenue	100
Other Expenses	40 - 60	40 - 60	Other Income	70
Undistributed Operating Expenses				
Administrative & General	65 - 85	15 - 35	Total Revenue	75
Marketing	65 - 85	15 - 35	Total Revenue	75
Franchise Fee	0	100	Occupancy	0
Prop. Operations & Maint.	55 - 75	25 - 45	Total Revenue	75
Energy	80 - 95	5 - 20	Total Revenue	75
Management Fee	0	100	Total Revenue	0
Fixed Expenses				
Property Taxes	100	0	Total Revenue	100
Insurance	100	0	Total Revenue	100
Reserve for Replacement	0	100	Total Revenue	0

Our fixed and variable projection model is based upon variables that we input for each revenue and expense item for a "base year," which in this case is 2003. The base-year forecast sets forth the ratios to revenue, amounts per available room, or amounts per occupied room that we believe can be achieved at the stated base-year average rate and occupancy. Our input variables are derived from the subject's historical operating performance and comparable hotel statements. The model then calculates a base-year forecast of income and expense in 2003 dollars. The actual forecast is derived by adjusting each year's revenue and expense by the amount fixed (the fixed expense multiplied by the inflated base-year amount) plus the variable amount (the variable expense multiplied by the inflated base-year amount) multiplied by the ratio of the projection year's occupancy to the base-year occupancy (in the case of departmental revenue and expense) or the ratio of the projection year's revenue to the base year's revenue (in the case of

undistributed operating expenses). Fixed expenses remain fixed, increasing only with inflation. Our discussion of the revenue and expense forecast in this report is based upon the output derived from the fixed and variable model. This forecast of revenue and expense is accomplished through a step-by-step approach, following the format of the *Uniform System of Accounts for Hotels*. Each category of revenue and expense is estimated separately and combined at the end in the final statement of income and expense.

Inflation Assumption

A general rate of inflation must be established that will be applied to most revenue and expense categories. The following table shows inflation estimates made by economists at some noted institutions and corporations.

Table 11-8 Inflation Estimates

Source	Projected Increase in Consumer Price Index (Annualized Rate Versus 12 Months Earlier)	
	May of 2004	November of 2003
Brian S. Wesbury, Griffin, Kubik	2.5 %	2.6 %
Lawrence Kudlow, Kudlow & Co.	2.0	2.3
Gail Fosler, Conference Board	2.6	2.5
Saul Hymans, University of Michigan	2.0	1.7
Gary Thayer, A.G. Edwards	2.1	2.3
Robert DiClemente, Citigroup	1.2	1.4
Susan M. Sterne, Economic Analysis	2.2	2.0
James F. Smith, University of North Carolina	1.4	1.0
Richard Rippe, Prudential Equity Group	1.7	1.9
David L. Littmann, Comerica Bank	2.3	2.0
Ian Shepherdson, High Frequency Economics	2.1	1.8
William T. Wilson, Ernst & Young	2.3	2.1
Neal Soss, CSFB	1.7	1.6
Joel L. Prakken, Macroeconomic Advisers	1.8	1.5
John Ryding/David Malpass, Bear Stearns	2.0	1.7
Stephen Gallagher, Societe Generale	2.2	2.0
Sung Won Sohn, Wells Fargo & Co.	1.2	1.4
Allen Sinai, Decision Economics	1.9	1.7
Peter Hooper, Deutsche Bank	1.9	1.5
Arun Raha, Eaton Corp.	2.6	2.4
Daniel Laufenberg, American Express	2.5	2.2
Douglas G. Duncan, Mortgage Bankers	1.5	NA
Henry Willmore, Barclays Capital	1.7	2.5
Shrouds & Fry, DuPont	2.1	2.0
J. Dewey Daane, Vanderbilt University	2.2	2.3
Maria Florini Ramirez, MFR Inc.	2.4	1.8
Nariman Behraves, Global Insight	1.5	1.9
David Lereah, Natl. Ass. of Realtors	1.6	1.7
David W. Berson, Fannie Mae	1.8	1.9
William B. Hummer, Wayne Hummer Invest.	1.4	2.3
Berner & Greenlaw, Morgan Stanley	1.6	1.8
David Resler, Nomura Securities	2.0	2.0
David Wyss, Standard & Poor's	1.5	1.9
Diane Swonk, Bank One	1.5	1.8
John Silvia, Wachovia	2.2	1.6
Mark Zandi, Economy.Com	1.7	1.7
McGee & Synnott, U.S. Trust	1.9	1.4
Nicholas S. Perna, Perna Associates	1.9	2.2
Ram Bhagavatula, The Royal Bank of Scotland	2.1	2.1
Richard DeKaser, National City Corporation	2.2	2.2
Donald H. Straszheim, Straszheim Advisors	2.0	2.0
Ethan Harris, Lehman Brothers	1.6	1.6
Paul Kasriel, Northern Trust Company	1.9	NA
Stuart G. Hoffman, PNC	2.3	2.2
Maury Harris, UBS	2.0	1.5
John Lonski, Moody's	2.5	2.2
Tracey Herrick, Jefferies & Co.	2.5	2.6
William C. Dudley, Goldman Sachs	1.7	1.7
Ellen Hughes-Cromwick, Ford Motor Company	2.0	NA
Kurt Karl, Swiss Re	1.4	1.4
Mickey D. Levy, Bank of America	1.6	2.0
Mike Cosgrove, Econoclast	1.2	1.5
Gene Huang, FedEx Corporation	2.2	NA
Edward Leamer, UCLA Anderson	2.1	NA
Averages	1.9 %	1.9 %
Actual Number as of November 30, 2003		1.8 %

Source: Wall Street Journal, January 2, 2004

As the preceding table indicates, the financial analysts who were surveyed anticipated inflation rates ranging from 1.2% to 2.6% (on an annualized basis) as of January 2004. A majority of the respondents estimate rates of 1.7% to 2.2%; the average is 1.9%. For the 12 months ending in November of 2003, the inflation forecasts ranged from 1.0% to 2.6% and the average was 1.9%. The actual inflation rate over that period was 1.8%.

As a further check on these inflation projections, we have reviewed historical increases in the Consumer Price Index (CPI). Because the value of real estate is predicated on cash flows over a relatively long period, inflation should be considered from a long-term perspective.

Table 11-9 National Consumer Price Index (All Urban Consumers)

Year	National Consumer Price Index	Percent Change from Previous Year
1994	148.2	---
1995	152.4	2.8 %
1996	156.9	3.0
1997	160.5	2.3
1998	163.0	1.6
1999	166.6	2.2
2000	172.2	3.4
2001	177.1	2.8
2002	179.9	1.6
2003	183.3	1.9
Average Annual Compounded Change,		
	1994 - 2003	2.4 %
	1999 - 2003	2.4

Source: Bureau of Labor Statistics

Between 1994 and 2003, the national CPI increased at an average annual compounded rate of 2.4%. The same rate was recorded in the more recent period from 1999 to 2003. In consideration of these historical trends, the projections set forth above, and our assessment of probable property appreciation levels, we have applied an underlying inflation rate of 2.5% to all appropriate revenue and expense items in the first two projection years and a 3.0% inflation rate throughout the remaining projection years. This stabilized

inflation rate takes into account normal, recurring inflation cycles. Inflation is likely to fluctuate above and below this level during the projection period.

Forecast of Income and Expense

The following description sets forth the basis for the forecast of income and expense. We anticipate that it will take four years for the subject property to reach a stabilized level of operation. Each revenue and expense item has been forecast based upon our review of the comparable income and expense statements and our industry knowledge. The following forecast is based upon calendar years beginning January 1, with the initial, partial year of operation based upon an assumed opening date of April 1, 2005. The forecast is expressed in inflated dollars for each year. At the start of our engagement, this appeared to be a reasonable estimate of the opening date of the proposed subject property assuming an accelerated development schedule. However, as of the date of this report, the assumed opening date may not be achieved. Our projections, however, assume the same timeline.

Rooms Revenue

Rooms revenue is determined by two variables: occupancy and average rate. Both were projected earlier in this report. The subject property is expected to stabilize with an occupancy level of 65.0% at an average rate of \$171.45 in the stabilized year. Following the stabilized year, the subject property's average rate is projected to increase at a level equal to the underlying rate of inflation.

Food Revenue

In the case of the subject property, food revenue is expected to be generated by a typical three-meal restaurant and room service operations. A significant component of the subject property's food revenue will result from its complete banqueting services, operating out of a centralized kitchen, to serve the roundly 25,000 square feet of meeting space. It is assumed that the management company will manage the food and beverage operations as well. The comparable conference center operating ratios indicate that, on average, food revenue accounts for 28.2% to 28.7% of total revenue.

Although food and beverage revenue varies directly with changes in occupancy, the portion generated by banquet sales and restaurant sales captured from outside the property is relatively fixed. The comparable operating statements indicate that food revenue ranged from 46.4% to 82.30% as a percentage of rooms revenue. We forecast food revenue at 52.2% of rooms revenue, in year one, stabilizing at roundly 45.9% of rooms revenue in the fourth year.

Beverage Revenue

Beverage revenue is generated by the sale of alcoholic beverages in a hotel's restaurants and banquet rooms and the sale of alcoholic and nonalcoholic

beverages in the property's bars and lounges. Alcoholic beverages included in room service operations are also classified as beverage revenue.

The comparable operating statements indicate that beverage revenue ranged from 9.7% to 30.8% as a percentage of food revenue. We forecast beverage revenue at 20.0% of food revenue throughout the projection period.

Telephone Revenue

Telephone revenue is generated by hotel guests who charge local and long-distance calls to their rooms, and by individuals who use the property's public telephones. Due to the use of cell phones by the traveling public, telephone revenues have been declining in recent years at lodging properties nationwide. In response to this trend, many hotels are attempting to replace this lost revenue with fee-based Internet access. This action is expected to stabilize telephone revenues.

Among the comparable hotels, telephone revenues ranged between \$1.88 and \$3.97 per occupied room, or between 1.6% and 4.0% of rooms revenue. We have forecast telephone revenue at \$122,000, or 2.0% of rooms revenue, in year one, stabilizing at \$175,000, or 1.7% of rooms revenue.

Conference Services Revenue

Conference services revenue refers to items relating to the operation of the conference center. Audiovisual equipment, meeting room rental, day-guest charges, and business-center services are all sources of conference service revenue. The vast majority of conference services revenue is generated by the sale of combined meeting packages (CMP). The CMP plan provides a marketing advantage to conference centers because most of the meeting costs can be determined in advance, allowing for efficient purchasing of materials and scheduling of staff, which enables operators to control costs. Furthermore, property management is able to forecast revenues more effectively than with hotels. Because executive conference centers are actually in the communications and education business, the availability of CMP plans, audiovisual equipment, and meeting facilities is an integral component of a particular property's differentiation and segmentation strategy. We estimate that 65% of all room nights sold in the meeting and group segment will be sold as part of a combined meeting package. Of those we estimate that \$60 per occupied room will be allocated to the conference services department.

Over the past three years, meeting planners have been price sensitive due to budgetary constraints imposed by their clients. We anticipate that this trend may have been persistent even as the economy improves thus limiting growth in conference services fees to inflationary levels. However, as meetings and

groups are forecast to constitute an increasingly large portion of total accommodated demand, conference services revenue is forecast to increase in relation to rooms revenues. Specifically, we have forecast conference services revenue at 11.7% of rooms revenue in the first projection year, stabilizing at 13.2% of rooms revenue in the fourth projection year. These figures are within the ratios indicated by the conference center comparable ratios, which show conference services ranging from 10.4% to 16.5% of total revenues.

Other Income

Other income is primarily derived from health club/spa revenues, parking revenues, and cancellation and attrition fees paid by groups. The remainder of the other revenue is composed of commissions from in-room movies, valet and laundry services, and vending machine commissions. We have projected other income at \$417,000, or 6.7% of rooms revenue in year one, stabilizing at \$519,000, or 5.0% of rooms revenue.

Rooms Expense

Rooms expense consists of items related to the sale and upkeep of guestrooms and public space. Salaries, wages, and employee benefits account for a substantial portion of this category. Although payroll varies somewhat with occupancy (because managers can schedule housekeepers, bell personnel, and house cleaners to work when demand requires), much of a hotel's payroll is fixed. Front desk personnel, public area cleaners, and the executive housekeeper and other supervisors are maintained at all times. As a result, salaries, wages, and employee benefits are only moderately sensitive to changes in occupancy.

Commissions and reservations are usually based on room sales, and thus are highly sensitive to changes in occupancy and average rate. While guest supplies vary 100% with occupancy, linen and other operating expenses are only slightly affected by volume.

Among the comparable hotels, rooms expense ranged from 22.0% to 27.1% of rooms revenue, or between \$26.18 and \$33.67 per occupied room. The conference center operating ratios indicated a more narrow range of between 24.0% and 25.1% of departmental revenues. We have projected a rooms expense ratio of 31.9% of rooms revenue in year one, stabilizing at 24.0% of rooms revenue in 2009/10.

Food and Beverage Expense

Food expense consists of those items necessary for the operation of a hotel's food and banquet facilities. Beverage expense consists of items necessary for the operation of a hotel's lounge and bar areas. The costs associated with beverage sales and payroll correlate highly with beverage revenues. Items

such as china, linen, and uniforms are less dependent on volume. Although the other expense items are basically fixed, they represent a relatively insignificant factor.

As mentioned, the advantage of offering combined meeting packages is that conference centers are able to capture food and beverage revenue that a traditional hotel might not capture. On the expense side, this also benefits the conference center, as the resulting economies of scale potentially reduce food and beverage expenses.

Among the comparable statements, food and beverage expense ranged from 61.6% to 103.0% of food and beverage revenue. The conference center comparables ranged from 70.1% to 75.5% of departmental income. We have projected a food and beverage expense ratio of 81.6% of departmental revenue in year one, stabilizing at 69.5% in 2009/10.

Telephone Expense

Telephone expense consists of all costs associated with this department. In the case of small hotels with automated systems, the operation of telephones may be an additional responsibility of front desk personnel; however, most large properties employ full-time operators. The bulk of telephone expense is related to the cost of local and long-distance calls billed by the telephone companies that provide these services. Because most calls are made by in-house guests, these costs are moderately correlated to occupancy.

Among the comparable statements, telephone expense ranged from 45.1% to 143.7% of telephone revenue. We have projected a telephone expense ratio of 83.0% of departmental revenue in year one, stabilizing at 70.0% in 2009/10.

Conference Services Expense

Conference services expense includes the payroll and benefits costs for the conference director and assistants, audiovisual technicians, and set-up housemen. Based on conference center comparable ratios, we have forecast the subject's conference services expense at 70.0% of departmental revenue in year one, stabilizing at 58.3% in 2009/10.

Other Income Expense

Other income expense consists of costs associated with generating other income revenue, and is dependent on the nature of the revenue sources. We have projected other income expense at 46.5% of departmental revenue in year one, stabilizing at 43.1% of departmental revenue in 2009/10.

Administrative and General Expense

Administrative and general expense includes the salaries and wages of all administrative personnel who are not directly associated with a particular

department. Expense items related to the management and operation of the property are also allocated to this category.

Most administrative and general expenses are relatively fixed. The exceptions are cash overages and shortages; commissions on credit card charges; provisions for doubtful accounts; and salaries, wages, and benefits, which are very slightly influenced by volume.

Among the comparable hotels, administrative and general expense ranged from 6.8% to 11.0% of total revenue. The conference center comparables state a similar range of 8.7% to 10.5% of total revenue. For the proposed subject property, administrative and general expense has been forecast at 11.5% of total revenue in 2006/07, stabilizing at 8.8% of total revenue in 2009/10.

Marketing Expense

Marketing expense consists of all costs associated with advertising, sales, and promotion; these activities are intended to attract and retain customers. Marketing can be used to create an image, develop customer awareness, and stimulate patronage of a property's various facilities. The marketing category is unique in that all expense items, with the exception of fees and commissions, are totally controlled by management. Most hotel operators establish an annual marketing budget that sets forth all planned expenditures. If the budget is followed, total marketing expense can be projected accurately.

Marketing expenditures are unusual because although there is a lag period before results are realized, the benefits are often extended over a long period. Depending on the type and scope of the advertising and promotion program implemented, the lag time can be as short as a few weeks or as long as several years. Marketing for conference centers is driven by relationships developed over time with meeting planners and other key decision-makers for large groups. As such, marketing a conference center is highly labor intensive. However, the favorable results of an effective marketing campaign tend to linger, and a property often enjoys the benefits of concentrated sales efforts for many months.

Among the comparable hotels, marketing expense ranged from 4.3% to 10.0% of total revenue. The conference center comparables state a more narrow marketing expense range from 6.8% to 7.7% of total revenue. Marketing expense has been forecast at 10.2% of total revenue in the first forecast year, stabilizing at 7.1% of total revenue in 2009/10.

Property Operations and Maintenance Expense

Property operations and maintenance expense is another expense category that is largely controlled by management. Except for repairs that are necessary to keep the facility open and prevent damage (e.g., plumbing, heating, and electrical items), most maintenance can be deferred for varying lengths of time.

Maintenance is an accumulating expense. If management elects to postpone performing a required repair, they have not eliminated or saved the expenditure; they have only deferred payment until a later date. A lodging facility that operates with a lower-than-normal maintenance budget is likely to accumulate a considerable amount of deferred maintenance.

The age of a lodging facility has a strong influence on the required level of maintenance. A new or thoroughly renovated property is protected for several years by modern equipment and manufacturers' warranties. However, as a hostelry grows older, maintenance expenses escalate. A well-organized preventive maintenance system often helps delay deterioration, but most facilities face higher property operations and maintenance costs each year, regardless of the occupancy trend. The quality of initial construction can also have a direct impact on future maintenance requirements. The use of high-quality building materials and construction methods generally reduces the need for maintenance expenditures over the long term. As the subject property will be newly constructed in its first year of operation, it is expected that property operations and maintenance expense will be moderate in the initial years of operation.

Among the comparable hotels, property operations and maintenance expense ranged between 3.9% and 8.2% of total revenue. The conference center comparables states an expense range from 4.5% to 6.1% of total revenue. Property operations and maintenance expense has been forecast at 3.8% of total revenue in the first year of operation, stabilizing at 3.6% of total revenue in 2009/10. Discounts were applied to the forecast expense levels to account for warranties and the newness of construction in the initial years of operation.

Energy Expense

The energy consumption of a lodging facility takes several forms including water and space heating, air conditioning, lighting, cooking fuel, and other miscellaneous power requirements. Total energy cost depends on the source and quantity of fuel used. Electricity tends to be the most expensive source, followed by oil and gas. This category also includes the cost of water service.

Among the comparables located in Arizona, energy expense ranged from \$6.90 to \$11.30 per occupied room, or from 3.3% to 4.9% of total revenue. Energy expense has been forecast at 4.2% of total revenue in the first projection year, stabilizing at 3.2% of total revenue in 2009/10.

Management Fee

Management expense consists of the fees paid to the management company contracted to operate the property. Some companies provide management services and a brand-name affiliation (first-tier management company), while others provide management services alone (second-tier management company). Some management contracts specify only a base fee (usually a percentage of total revenue), while others call for both a base fee and an incentive fee (usually a percentage of defined profit). Basic hotel management fees are almost always based on a percentage of total revenue, which means they have no fixed component. While base fees typically range from 2% to 4% of total revenue, incentive fees are deal specific and often are calculated as a percentage of income available after debt service and, in some cases, after a preferred return on equity.

Due to the deal specificity of the incentive portion of the management fee, total management fees are difficult to hypothesize without a specific management agreement in hand. Even then, the ownership structure and debt level of a deal may ultimately impact the fees paid. HVS International monitors current trends in management agreements and is familiar with the current range of total management costs.

We are finding that in today's market, total management fees for a first-tier conference center management company range from 2% to 4% of total revenue. Management fees for the subject property have been forecast at 3.0% of total revenue, assuming that a first-tier conference center management company operates the property.

Property Taxes

Property (or ad valorem) tax is one of the primary revenue sources of municipalities. A system of assessments is established based on the concept that the tax burden should be distributed in proportion to the value of all properties within a taxing jurisdiction. Theoretically, the assessed value placed on each parcel bears a definite relationship to market value, so properties with equal market values will have similar assessments and properties with higher and lower values will have proportionately larger and smaller assessments. Depending on the taxing policy of the municipality, property taxes can be based on the value of the real property or the value of the personal property and the real property.

The taxing jurisdiction governing the subject property assesses real and personal property. The assessed value ratio is reported to be approximately 25% of market value for commercial property. The assessed value ratio for vacant land is 16% and for owner occupied or rentals is 10%. An estimation of market value is a matter of determining the price a typical buyer would pay for a property in its present condition. Some factors the assessor considers are: what similar properties are selling for, what it would cost to replace your property, the rent it may earn, and any other factors that affect value. Market value is defined as the amount a typical, well-informed purchaser would be willing to pay for a property. Construction cost is an historical figure which may or may not reflect the current market value of a property.

Because the objective of assessed value is to maintain a specific value relationship among all properties in a taxing jurisdiction, comparable hotel assessments should be evaluated to determine whether the subject property's assessed value is equitable. A review of the assessed value of the primary and secondary competitors of the proposed subject property, located in the City of Flagstaff taxing jurisdiction, reveals the following information.

Table 11-10 Total Assessed Value of Comparable Hotels

Hotel	Number of Rooms	Total Market Value Assessment	Market Value Assessment per Room
Little America	246	\$13,339,238	\$54,225
Radisson Woodlands	183	7,197,052	39,328
Embassy Suites	119	5,203,881	43,730
Hilton Garden Inn	90	3,031,405	33,682
Residence Inn	102	4,000,000	39,216
Hampton Inn	50	1,549,102	30,982
Hampton Inn & Suites	126	4,787,938	38,000
Proposed Subject Property	250	\$20,334,204	\$81,337 *

Source: Coconino Tax Assessor's Office

* 150% of Little America's Assessment per Room

The improvements of the proposed subject property are expected to be of a significantly higher quality than that which currently exists in the lodging supply of Flagstaff. As such, the per-room assessments for the proposed subject property are expected to be roughly 150% higher than the assessment of the Little America, the highest assessed value per room in Flagstaff.

Total property taxes are the combination of the primary and secondary tax rates, which differ depending upon the tax area code that a particular property is located in. The primary taxes include state, county, city taxes, school district taxes, and community college districts taxes. The secondary taxes are to cover bonded indebtedness and voter approved districts. The current tax rates applicable to the proposed subject property are presented in the following table.

Table 11-11 Tax Rates Applicable to the Proposed Subject Property

City of Flagstaff Jurisdiction	Tax Rate per \$100 of Assessment
Primary Rate	6.9369
Secondary Rate	<u>2.9581</u>
Total:	9.8950

Commercial personal property is also taxed in Coconino County at the prevailing tax rates for land and improvements. Personal property assessment relies upon the honor system for reporting the personal property acquired and the year and original cost of acquisition. Personal property is valued by the cost approach by first adjusting to the replacement cost and then depreciating for the age of the item.

It is assumed that the property tax rates will remain constant throughout the projection period and that property assessed values will increase with the underlying rate of inflation. Therefore, it is assumed that property taxes will increase at the underlying rate of inflation.

We estimate that conventional property taxes for the proposed conference center hotel would equal roundly \$523,000 in the first projection year, increasing to roundly \$572,000 in the stabilized year. However, the property tax forecast for the proposed subject property is uncertain as it has yet to be determined exactly how the subject site land will be conveyed to the development team, and whether it will be part of a long-term ground lease or if there will be a sale. Additionally, a representative of the City of Flagstaff has indicated that it is possible to arrange for complete property tax abatement for the subject property for up to 8 years. However, complete property tax abatement may not be possible and this deal may require either a lump-sum or annual payment in lieu of taxes. For the purposes of this analysis we have not included property taxes during the first 8 projection years and included

property taxes in the 9th and 10th years, adjusted only for inflation from the stabilized year. We note that this is a preliminary estimate subject to change.

Insurance Expense

The insurance expense category consists of the cost of insuring the hotel and its contents against damage or destruction by fire, weather, sprinkler leakage, boiler explosion, plate glass breakage, and so forth. General insurance costs also include premiums relating to liability, fidelity, and theft coverage. It does not include liability coverage, which is a component of administrative and general expense.

Insurance rates are based on many factors, including building design and construction, fire detection and extinguishing equipment, fire district, distance from the firehouse, and the area's fire experience. Insurance expenses do not vary with occupancy. Insurance rates for hotels remained relatively low throughout the latter half of the 1990s, as competition among the insurance companies kept price increases to a minimum in most markets. In 2001, insurance rates began to increase substantially. The terrorist attacks of September 11th have strained the financial resources of the insurance and reinsurance industries, resulting in further increases in insurance costs. As a result, premiums have increased by anywhere from 25% to 100%, but are beginning to moderate.

The *HOST Report* notes an insurance expense range from \$389 to \$571 per available room. We have projected an insurance expense of \$378 per available room in 2006/07 and \$413 per available room in the stabilized year 2009/10.

Reserve for Replacement

Furniture, fixtures, and equipment are essential to the operation of a lodging facility. This category includes all non-real estate items that are capitalized, rather than expensed. The furniture, fixtures, and equipment of a hotel are exposed to heavy use and must be replaced at regular intervals. The useful life of these items is determined by their quality, durability, and the amount of guest traffic and use.

Maintenance is an accumulating expense. If management elects to postpone performing a required procedure, the expenditure has not been eliminated or saved, but only deferred payment until a later date. The age of a lodging facility greatly influences the required level of maintenance. A new or thoroughly renovated property is protected for several years by modern equipment and manufacturers' warranties. A well-organized preventive maintenance program often helps delay deterioration, but most facilities face

higher property operations and maintenance costs each year, regardless of the occupancy trend.

The International Society of Hospitality Consultants (ISHC) undertook a major industry-sponsored study of the capital expenditure requirements for full-service and limited-service hotels. The findings of the study were published in reports in 1995¹ and 2000.² The historical capital expenditures of well-maintained hotels were investigated through the compilation of data provided by most of the major hotel companies in the United States. A prospective analysis of future capital expenditure requirements was also performed based upon the cost to replace short- and long-lived building components over a hotel's economic life. The study showed that the capital expenditure requirements for hotels vary significantly from year and depend upon both the actual and effective age of a property. Based on the results of this study, it is our opinion that hotel lenders and investors now are requiring reserves for replacement ranging from 4% to 5% of total revenue.

Periodic replacement of furniture, fixtures, and equipment is essential to maintain the quality, image, and income-producing potential of a lodging facility. Because capitalized expenditures are not included in the operating statement but nevertheless affect an owner's cash flow, analysis should reflect these expenses in the form of an appropriate reserve for replacement.

Based on the subject property's age and condition, we estimate that a reserve for replacement of 1.0% in the first year, increasing annually to 5.0% in the fifth forecast year, is sufficient to provide for the timely and periodic replacement of the subject property's furniture, fixtures, and equipment.

Summary of Projections

Based on the preceding analysis, we have formulated a forecast of income and expense. The following table presents a detailed forecast through the stabilized year, including amounts per available room and per occupied room. The second table illustrates our 10-year forecast of income and expense, presented with a lesser degree of detail. The forecast is based upon fiscal years beginning April 1, 2006. The forecast is expressed in inflated dollars for each year.

¹ The International Society of Hotel Consultants, *CapEx, A Study of Capital Expenditure in the U.S. Hotel Industry*, 1995.

² The International Society of Hotel Consultants, *CapEx 2000, A Study of Capital Expenditure in the U.S. Hotel Industry*.

Table 11-12 Detailed Forecast of Income and Expense, Proposed Conference Center Hotel, Flagstaff, Arizona

	2006/07				2007/08				2008/09				Stabilized			
Number of Rooms:	250				250				250				250			
Occupancy:	48%				56%				63%				65%			
Average Rate:	\$142.84				\$154.31				\$166.17				\$171.45			
RevPAR:	\$68.56				\$86.41				\$104.68				\$111.44			
Days Open:	365				365				365				365			
Occupied Rooms:	43,800	%Gross	PAR	POR	51,100	%Gross	PAR	POR	57,488	%Gross	PAR	POR	59,313	%Gross	PAR	POR
REVENUE																
Rooms	\$6,257	54.6 %	\$25,028	\$142.85	\$7,885	55.5 %	\$31,540	\$154.31	\$9,552	57.0 %	\$38,208	\$166.16	\$10,169	57.0 %	\$40,676	\$171.45
Food	3,266	28.5	13,064	74.57	3,851	27.1	15,405	75.37	4,406	26.3	17,624	76.64	4,667	26.2	18,670	78.69
Beverage	669	5.8	2,677	15.28	804	5.7	3,218	15.74	920	5.5	3,681	16.01	975	5.5	3,900	16.44
Telephone	122	1.1	490	2.79	144	1.0	577	2.82	165	1.0	661	2.87	175	1.0	700	2.95
Conference Services	730	6.4	2,920	16.67	1,063	7.5	4,251	20.80	1,218	7.3	4,872	21.19	1,344	7.5	5,377	22.66
Other Income	417	3.6	1,667	9.51	455	3.2	1,820	8.91	485	2.9	1,938	8.43	504	2.8	2,015	8.49
Total Revenues	11,461	100.0	45,846	261.68	14,203	100.0	56,813	277.95	16,746	100.0	66,984	291.30	17,834	100.0	71,337	300.68
DEPARTMENTAL EXPENSES *																
Rooms	1,997	31.9	7,987	45.59	2,170	27.5	8,678	42.46	2,337	24.5	9,346	40.64	2,437	24.0	9,746	41.08
Food & Beverage	3,210	81.6	12,840	73.29	3,490	75.0	13,962	68.31	3,761	70.6	15,045	65.43	3,923	69.5	15,692	66.14
Telephone	102	83.0	406	2.32	110	76.0	439	2.15	118	71.2	471	2.05	123	70.0	490	2.07
Conference Services	511	70.0	2,044	11.67	682	64.2	2,728	13.35	746	61.3	2,984	12.98	784	58.3	3,136	13.22
Other Expenses	194	46.5	776	4.43	202	44.4	808	3.95	210	43.4	841	3.66	217	43.1	868	3.66
Total	6,013	52.5	24,053	137.29	6,654	46.8	26,616	130.21	7,172	42.8	28,686	124.75	7,483	42.0	29,933	126.17
DEPARTMENTAL INCOME	5,448	47.5	21,793	124.39	7,549	53.2	30,197	147.73	9,575	57.2	38,298	166.55	10,351	58.0	41,404	174.52
UNDISTRIBUTED OPERATING EXPENSES																
Administrative & General	1,320	11.5	5,278	30.13	1,414	10.0	5,658	27.68	1,506	9.0	6,025	26.20	1,565	8.8	6,260	26.39
Marketing	1,172	10.2	4,690	26.77	1,200	8.4	4,798	23.48	1,217	7.3	4,866	21.16	1,264	7.1	5,056	21.31
Prop. Operations & Maint.	436	3.8	1,746	9.97	526	3.7	2,105	10.30	592	3.5	2,366	10.29	647	3.6	2,588	10.91
Energy	482	4.2	1,929	11.01	517	3.6	2,067	10.11	550	3.3	2,201	9.57	572	3.2	2,287	9.64
Total	3,411	29.7	13,643	77.87	3,657	25.7	14,629	71.57	3,865	23.1	15,459	67.23	4,048	22.7	16,192	68.25
HOUSE PROFIT	2,038	17.8	8,150	46.52	3,892	27.5	15,568	76.16	5,710	34.1	22,840	99.32	6,303	35.3	25,213	106.27
Management Fee	344	3.0	1,375	7.85	426	3.0	1,704	8.34	502	3.0	2,010	8.74	535	3.0	2,140	9.02
INCOME BEFORE FIXED CHARGES	1,694	14.8	6,775	38.67	3,466	24.5	13,863	67.82	5,208	31.1	20,830	90.59	5,768	32.3	23,073	97.25
FIXED EXPENSES																
Property Taxes	0	0.0	0	0.00	0	0.0	0	0.00	0	0.0	0	0.00	0	0.0	0	0.00
Insurance	94	0.8	378	2.16	97	0.7	389	1.90	100	0.6	401	1.74	103	0.6	413	1.74
Reserve for Replacement	115	1.0	458	2.62	284	2.0	1,136	5.56	502	3.0	2,010	8.74	713	4.0	2,853	12.03
Total	209	1.8	836	4.77	381	2.7	1,525	7.46	603	3.6	2,410	10.48	817	4.6	3,266	13.77
NET INCOME	\$1,485	13.0 %	\$5,938	\$33.89	\$3,084	21.8 %	\$12,338	\$60.36	\$4,605	27.5 %	\$18,420	\$80.10	\$4,952	27.7 %	\$19,806	\$83.48

*Departmental expenses are expressed as a percentage of departmental revenues.

Table 11-13 Ten-Year Forecast of Income and Expense, Proposed Conference Center Hotel, Flagstaff, Arizona

	2006/07		2007/08		2008/09		2009/10		2010/11		2011/12		2012/13		2013/14		2014/15		2015/16	
Number of Rooms:	250		250		250		250		250		250		250		250		250		250	
Occupied Rooms:	43,800		51,100		57,488		59,313		59,313		59,313		59,313		59,313		59,313		59,313	
Occupancy:	48%		56%		63%		65%		65%		65%		65%		65%		65%		65%	
Average Rate:	\$142.84	% of	\$154.31	% of	\$166.17	% of	\$171.45	% of	\$176.59	% of	\$181.89	% of	\$187.35	% of	\$192.97	% of	\$198.75	% of	\$204.72	% of
RevPAR:	\$68.56	Gross	\$86.41	Gross	\$104.68	Gross	\$111.44	Gross	\$114.78	Gross	\$118.23	Gross	\$121.77	Gross	\$125.43	Gross	\$129.19	Gross	\$133.07	Gross
REVENUE																				
Rooms	\$6,257	54.6 %	\$7,885	55.5 %	\$9,552	57.0 %	\$10,169	57.0 %	\$10,474	57.0 %	\$10,788	57.0 %	\$11,112	57.0 %	\$11,445	57.0 %	\$11,789	57.0 %	\$12,142	57.0 %
Food	3,266	28.5	3,851	27.1	4,406	26.3	4,667	26.2	4,808	26.2	4,952	26.2	5,100	26.2	5,253	26.2	5,411	26.2	5,573	26.2
Beverage	669	5.8	804	5.7	920	5.5	975	5.5	1,004	5.5	1,034	5.5	1,065	5.5	1,097	5.5	1,130	5.5	1,164	5.5
Telephone	122	1.1	144	1.0	165	1.0	175	1.0	180	1.0	186	1.0	191	1.0	197	1.0	203	1.0	209	1.0
Conference Services	730	6.4	1,063	7.5	1,218	7.3	1,344	7.5	1,384	7.5	1,426	7.5	1,469	7.5	1,513	7.5	1,558	7.5	1,605	7.5
Other Income	417	3.6	455	3.2	485	2.9	504	2.8	519	2.8	534	2.8	550	2.8	567	2.8	584	2.8	601	2.8
Total	11,461	100.0	14,203	100.0	16,746	100.0	17,834	100.0	18,369	100.0	18,920	100.0	19,488	100.0	20,072	100.0	20,675	100.0	21,295	100.0
DEPARTMENTAL EXPENSES*																				
Rooms	1,997	31.9	2,170	27.5	2,337	24.5	2,437	24.0	2,510	24.0	2,585	24.0	2,663	24.0	2,742	24.0	2,825	24.0	2,909	24.0
Food & Beverage	3,210	81.6	3,490	75.0	3,761	70.6	3,923	69.5	4,041	69.5	4,162	69.5	4,287	69.5	4,415	69.5	4,548	69.5	4,684	69.5
Telephone	102	83.0	110	76.0	118	71.2	123	70.0	126	70.0	130	70.0	134	70.0	138	70.0	142	70.0	146	70.0
Conference Services	511	70.0	682	64.2	746	61.3	784	58.3	808	58.3	832	58.3	857	58.3	883	58.3	909	58.3	936	58.3
Other Expenses	194	46.5	202	44.4	210	43.4	217	43.1	224	43.1	230	43.1	237	43.1	244	43.1	252	43.1	259	43.1
Total	6,013	52.5	6,654	46.8	7,172	42.8	7,483	42.0	7,708	42.0	7,939	42.0	8,177	42.0	8,422	42.0	8,675	42.0	8,935	42.0
DEPARTMENTAL INCOME	5,448	47.5	7,549	53.2	9,575	57.2	10,351	58.0	10,662	58.0	10,981	58.0	11,311	58.0	11,650	58.0	12,000	58.0	12,359	58.0
UNDISTRIBUTED OPERATING EXPENSES																				
Administrative & General	1,320	11.5	1,414	10.0	1,506	9.0	1,565	8.8	1,612	8.8	1,660	8.8	1,710	8.8	1,761	8.8	1,814	8.8	1,869	8.8
Marketing	1,172	10.2	1,200	8.4	1,217	7.3	1,264	7.1	1,302	7.1	1,341	7.1	1,381	7.1	1,423	7.1	1,465	7.1	1,509	7.1
Prop. Operations & Maint.	436	3.8	526	3.7	592	3.5	647	3.6	666	3.6	686	3.6	707	3.6	728	3.6	750	3.6	773	3.6
Energy	482	4.2	517	3.6	550	3.3	572	3.2	589	3.2	607	3.2	625	3.2	644	3.2	663	3.2	683	3.2
Total	3,411	29.7	3,657	25.7	3,865	23.1	4,048	22.7	4,169	22.7	4,294	22.7	4,423	22.7	4,556	22.7	4,693	22.7	4,833	22.7
HOUSE PROFIT	2,038	17.8	3,892	27.5	5,710	34.1	6,303	35.3	6,492	35.3	6,687	35.3	6,888	35.3	7,094	35.3	7,307	35.3	7,526	35.3
Management Fee	344	3.0	426	3.0	502	3.0	535	3.0	551	3.0	568	3.0	585	3.0	602	3.0	620	3.0	639	3.0
INCOME BEFORE FIXED CHARGES	1,694	14.8	3,466	24.5	5,208	31.1	5,768	32.3	5,941	32.3	6,119	32.3	6,303	32.3	6,492	32.3	6,687	32.3	6,887	32.3
FIXED EXPENSES																				
Property Taxes	0	0.0	0	0.0	0	0.0	0	0.0	0	0.0	0	0.0	0	0.0	0	0.0	663	3.2	683	3.2
Insurance	94	0.8	97	0.7	100	0.6	103	0.6	106	0.6	110	0.6	113	0.6	116	0.6	120	0.6	123	0.6
Reserve for Replacement	115	1.0	284	2.0	502	3.0	713	4.0	918	5.0	946	5.0	974	5.0	1,004	5.0	1,034	5.0	1,065	5.0
Total	209	1.8	381	2.7	603	3.6	817	4.6	1,025	5.6	1,056	5.6	1,087	5.6	1,120	5.6	1,816	8.8	1,871	8.8
NET INCOME	\$1,485	13.0 %	\$3,084	21.8 %	\$4,605	27.5 %	\$4,952	27.7 %	\$4,916	26.7 %	\$5,064	26.7 %	\$5,216	26.7 %	\$5,372	26.7 %	\$4,871	23.5 %	\$5,016	23.5 %

*Departmental expenses are expressed as a percentage of departmental revenues.

The forecast of income and expense for the proposed subject property indicates that net income will improve from 13.0% of total revenue in the first forecast year to stabilize at 26.7% of total revenue, allowing for a 5.0% reserve for replacement. This increase in profitability is forecast to be partly achieved through a decrease in total departmental expenses, from 52.5% of departmental revenues in the first forecast year to 42.0% of departmental revenues in the stabilized year. Additionally, undistributed operating expenses are forecast to decrease from 29.7% of total revenue in the first forecast year to 22.7% of total revenue in the stabilized year.

12. Statement of Assumptions and Limiting Conditions

1. This report is to be used in whole and not in part.
2. No responsibility is assumed for matters of a legal nature.
3. We have not considered the presence of potentially hazardous materials such as asbestos, urea formaldehyde foam insulation, any form of toxic waste, polychlorinated biphenyls (PCBs), pesticides, mold, or lead-based paints. The appraisers are not qualified to detect hazardous substances, and we urge the client to retain an expert in this field if desired.
4. We have made no survey of the property, and we assume no responsibility in connection with such matters. Sketches, photographs, maps, and other exhibits are included to assist the reader in visualizing the property. It is assumed that the use of the land and improvements is within the boundaries of the property described, and that there is no encroachment or trespass unless noted.
5. All information, estimates, and opinions obtained from parties not employed by HVS International are assumed to be true and correct. We can assume no liability resulting from misinformation.
6. Unless noted, we assume that there are no encroachments, zoning violations, or building violations encumbering the subject property.
7. All mortgages, liens, encumbrances, leases, and servitudes have been disregarded unless specified otherwise.
8. None of this material may be reproduced in any form without our written permission, and the report cannot be disseminated to the public through advertising, public relations, news, sales, or other media.
9. We are not required to give testimony or attendance in court by reason of this analysis without previous arrangements, and only when our standard per diem fees and travel costs are paid prior to the appearance.

10. If the reader is making a fiduciary or individual investment decision and has any questions concerning the material presented in this report, it is recommended that the reader contact us.
11. We take no responsibility for any events or circumstances that take place subsequent to the date of our field inspection.
12. The quality of a lodging facility's on-site management has a direct effect on a property's economic viability. The financial forecasts presented in this analysis assume responsible ownership and competent management. Any departure from this assumption may have a significant impact on the projected operating results.
13. The estimated operating results presented in this report are based on an evaluation of the overall economy, and neither take into account nor make provision for the effect of any sharp rise or decline in local or national economic conditions. To the extent that wages and other operating expenses may advance during the economic life of the property, we expect that the prices of rooms, food, beverages, and services will be adjusted to at least offset those advances. We do not warrant that the estimates will be attained, but they have been prepared on the basis of information obtained during the course of this study and are intended to reflect the expectations of a typical hotel buyer.
14. This analysis assumes continuation of all Internal Revenue Service tax code provisions as stated or interpreted on the date of our field inspection.
15. Many of the figures presented in this report were generated using sophisticated computer models that make calculations based on numbers carried out to three or more decimal places. In the interest of simplicity, most numbers have been rounded to the nearest tenth of a percent. Thus, these figures may be subject to small rounding errors.
16. It is agreed that our liability to the client is limited to the amount of the fee paid as liquidated damages. Our responsibility is limited to the client, and use of this report by third parties shall be solely at the risk of the client and/or third parties. The use of this report is also subject to the terms and conditions set forth in our engagement letter with the client.
17. This report was prepared by HVS International. All opinions, recommendations, and conclusions expressed during the course of this

assignment are rendered by the staff of H&R Valuation Services, Inc. as employees, rather than as individuals.

18. This report is set forth as a market study of the proposed subject property; this is not an appraisal report.
19. This analysis assumes that the development and planning of the subject property prior to opening have been competently managed. Among the items assumed to occur are the employment of management and executive positions, the hiring and training of hotel staff, the establishment and implementation of operating policies and procedures, and the production and execution of a sales and marketing plan. The projections in this analysis are dependent upon a typical pre-opening process. Any variance from industry pre-opening planning and process for a hotel of this nature may materially affect the value(s) set forth in this report.
20. This analysis assumes that the subject property will not be responsible for property taxes during the first eight projection years of operation. We have included property taxes in our forecast of the ninth and tenth years of operation adjusted only for inflation from the stabilized year. We note that this is a preliminary estimate subject to change.
21. This analysis assumes an opening date of April 1, 2005. At the start of our engagement, this appeared to be a reasonable estimate of the opening date of the proposed subject property assuming an accelerated development schedule. However, as of the date of this report, the assumed opening date not be achieved. Our projections, however, assume the same timeline.

13. Certification

We, the undersigned, hereby certify:

1. that the statements of fact presented in this report are true and correct to the best of our knowledge and belief;
2. that the reported analyses, opinions, and conclusions presented in this report are limited only by the assumptions and limiting conditions set forth, and are our personal, impartial, and unbiased professional analyses, opinions, and conclusions;
3. that Stephen O'Connor, Elaine Sahlins, and Hans Detlefsen personally inspected the market area described in this report; Thomas Hazinski participated in the analysis, but did not personally inspect the market area;
4. that we have no current or contemplated interests in the real estate that is the subject of this report;
5. that we have no personal interest or bias with respect to the subject matter of this report or the parties involved;
6. that this report sets forth all of the limiting conditions (imposed by the terms of this assignment) affecting the analyses, opinions, and conclusions presented herein;
7. that the fee paid for the preparation of this report is not contingent upon our conclusions, or the occurrence of a subsequent event directly related to the intended use of this report;
8. that our engagement in this assignment was not contingent upon developing or reporting predetermined results; and
9. that no one other than those listed above and the undersigned prepared the analyses, conclusions, and opinions concerning the real estate that are set forth in this market study.

Stephen O'Connor
Associate

Elaine Sahlins
Director

Hans Detlefsen
Senior Manager

Thomas Hazinski
Managing Director

SO:ES:HD:TH